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No.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

MOUNTAIN PLAINS CONGRESS OF SENIOR ORGANIZATIONS; MR. & MRS. HUGH A. GROVES; FRANCIS SEELY; ESTELLE WHITTLE; HENRY WHITTLE; MR. & MRS. BURTON W. ATKINSON; MR. & MRS. C.E. DIETRICH; HARRIET MILLER; and ALICE VAN LANDINGHAM,

Petitioners,

v.

NATHAN MALCHMAN, GERTA CONWAY, WILLIAM DEAUTRIELL and LOUIS STONE,

and

LEONARD DAVIS, SOPHIE DAVIS, COLONIAL PENN GROUP, INC., COLONIAL PENN FRANKLIN INSURANCE COMPANY, INTRAMERICA LIFE INSURANCE COMPANY, NATIONAL ASSOCIATION PLANS, INC., AMERICAN ASSOCIATION OF RETIRED PERSONS, NATIONAL RETIRED TEACHERS ASSOCIATION, CARRIE B. ALLEN, ORANDA BANGSBERG, BERNARD BERGGREN, JUNE BIGGAR, ARTHUR BOUTON, OLAF KAASA, CLARA L. KLEWENO, FLOYD E. TUMBLESON, J. LEONARD JOHNSON, C.E. CARMICHAEL, AMERICAN ASSOCIATION OF RETIRED PERSONS INSURANCE TRUST, DOROTHY M. CRIPPEN, JAMES J. BROWNING, LLOYD I. SINGER, CYRIL F. BRICKFIELD and JOHN J. MacWILLIAMS,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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QUESTIONS PRESENTED FOR REVIEW

1. Do Rule 23 of the Federal Rules of Civil Procedure and the Due Process Clause prohibit class counsel from conducting negotiations regarding their attorney fees while negotiating substantive matters affecting the rights of absentee class members?

2. Do Rule 23 of the Federal Rules of Civil Procedure and the Due Process Clause preclude approval of a class action settlement where class counsel and the purported class representatives have familial and other close personal relationships?

3. Should 11.2 million class members be bound by the terms of a settlement which extinguishes valuable damage claims when objectors to the settlement have been denied discovery and an evidentiary hearing regarding the adequacy and fairness of the settlement and the manner in which settlement negotiations were conducted?

4. Should class certification tentatively agreed upon by the parties solely for settlement purposes be denied when the class representatives and defendants agree to expand the class nearly five-fold to bar future actions by persons never represented in the litigation?

LIST OF PARTIES

All formal parties to the proceedings are listed in the caption of the case in this Court. Petitioner Mountain Plains Congress of Senior Citizen Organizations represents several senior citizen organizations in the Western United States which constituent organizations have more than forty thousand members.

Not listed as parties but nevertheless bound by the orders and decisions herein are 11.2 million class members including approximately 10.5 million members of the American Association of Retired Persons ("AARP"), approximately 400,000 members of the National Retired Teachers Association ("NRTA") and approximately 300,000 persons who are members of AARP's pre-retirement unit known as Action For an Independent Maturity ("AIM").

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NATHAN MALCHMAN, GERTA CONWAY, WILLIAM DEAUTRIELL and LOUIS STONE,

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LEONARD DAVIS, SOPHIE DAVIS, COLONIAL PENN GROUP, INC., COLONIAL PENN FRANKLIN INSURANCE COMPANY, INTRAMERICA LIFE INSURANCE COMPANY, NATIONAL ASSOCIATION PLANS, INC., AMERICAN ASSOCIATION OF RETIRED PERSONS, NATIONAL RETIRED TEACHERS ASSOCIATION, CARRIE B. ALLEN, ORANDA BANGSBERG, BERNARD BERGGREN, JUNE BIGGAR, ARTHUR BOUTON, OLAF KAASA, CLARA L. KLEWENO, FLOYD E. TUMBLESON, J. LEONARD JOHNSON, C.E. CARMICHAEL, AMERICAN ASSOCIATION OF RETIRED PERSONS INSURANCE TRUST, DOROTHY M. CRIPPEN, JAMES J. BROWNING, LLOYD I. SINGER, CYRIL F. BRICKFIELD and JOHN J. MacWILLIAMS,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Mountain Plains Congress of Senior Organizations, et al., respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Second Circuit in *Malchman, et al. v. Davis, et al.*, Nos. 84-7589 and 84-7669 (decided May 10, 1985).

OPINIONS BELOW

The Opinion of the United States District Court for the Southern District of New York is reported at 588 F.Supp. 1047 and is appended hereto as Appendix B. The three separate panel opinions of the Second Circuit for which review is sought are reported at 761 F.2d 843 and are appended hereto as Appendix A. The court of appeals' earlier decision in this case, remanding the cause to the district court, is reported at 706 F.2d 426 and is appended hereto as Appendix C.

JURISDICTION

The court below issued its opinions on May 10, 1985. A timely petition for rehearing and suggestion for rehearing *en banc* was denied on June 20, 1985. This Court has jurisdiction pursuant to 28 U.S.C. §1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

Rule 23 of the Federal Rules of Civil Procedure provides, in relevant part, as follows:

> (a) PREREQUISITES TO CLASS ACTION. One or more members of a class may sue or be sued as representative parties on behalf of all only if (1) the class is so numerous that joinder of all members is impracticable, (2) there are questions of law or fact common to the class, (3) the claims or defenses of the representative parties are typical of the claims or defenses of the class, and (4) the representative parties will fairly and adequately protect the interests of the class.
>
> (b) CLASS ACTIONS MAINTAINABLE. An action may be maintained as a class action if the prerequisites of subdivision (a) are satisfied
>
> . . . .

* * *

(c) DETERMINATION BY ORDER WHETHER CLASS ACTION TO BE MAINTAINED; NOTICE: JUDGMENT: ACTIONS CONDUCTED PARTIALLY AS CLASS ACTIONS.

(1) As soon as practicable after the commencement of an action brought as a class action, the court shall determine by order whether it is to be so maintained. An order under this subdivision may be conditional, and may be altered or amended before the decision on the merits.

* * *

(e) DISMISSAL OR COMPROMISE. A class action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to all members of the class in such manner as the court directs.

The Fifth Amendment to the United States Constitution provides in pertinent part as follows:

"No person shall . . . be deprived of life, liberty, or property, without due process of law."

STATEMENT OF THE CASE

This case involves settlement of the largest class action ever. It also involves five serious abuses of the class action device:

(1) negotiation of unusually generous attorneys' fees for class counsel simultaneously with negotiation of substantive issues affecting the class;

(2) putative class representatives with familial

and other close personal relationships with class counsel;

(3) use of the tentative class certification device to sweep under the carpet serious questions which had been raised regarding the adequacy of the class representatives but which were never considered by the district court in an adversary setting;

(4) the preclusion of potentially huge damage claims in exchange for defendants' agreement to give "free sailing" to class counsel's large fee request; and

(5) the expansion of the class more than fourfold so as to achieve the broadest possible preclusion of possible future claims.

While any one of these abuses should have provided ample basis for rejecting this proposed settlement, their cumulative effect is an unprecedented perversion of the class action device. Instead of assuring the fullest possible disclosure of the facts pertaining to each of these defects, the lower courts compounded the problem by denying any discovery to objectors and refusing to permit or require an evidentiary hearing regarding these matters and the fairness of the settlement.

All three Circuit Judges on the Second Circuit panel recognized the grievious wrong done to the 11,200,000 class members by this settlement, but all three divided on what should be done about it. Circuit Judge Oakes, who authored the panel's principal opinion, acknowledged that the settlement agreement here "amounted to little more than a trade of damages relief foreclosure for attorneys'

fees" (App. 20a). Circuit Judge Newman condemned, as fraught with potential abuse, "clear sailing" agreements where defendants agree not to oppose a fee award up to a certain sum (App. 31a). Though finding that precisely such an agreement had occurred here, Judges Newman and Oakes affirmed the district court's order with one minor modification. In dissent, Circuit Judge Mansfield bluntly concluded that the settlement agreement negotiated here "is tainted by the simultaneously-negotiated agreement by the defendants not to oppose their paying $2,325,000 to class counsel" (App. 32a).

STATEMENT OF FACTS[1]

A. Inception of the Relationship Between AARP-NRTA and Colonial Penn.

In the mid-1950's, Respondent Leonard Davis, who had been formally barred from selling insurance in New York, met the late Ethyl Percy Andrus, the founder of NRTA. At Andrus' request, Davis agreed to locate and persuade an insurance company to underwrite and offer health insurance coverage to elderly retired teachers (App. 78a). Davis found a company which agreed to write such insurance and, with NRTA's endorsement and assistance, Davis aggressively sold such insurance to NRTA's members. His efforts were highly profitable (App. 78a).

Davis later agreed to sponsor and underwrite the formation of a new organization for senior citizens – a sister "nonprofit" association of NRTA not limited to former

[1]The facts recited herein are taken largely from the court of appeals' opinions. The district court never made any findings on the essential background facts.

teachers — which became known as the American Association of Retired Persons. Davis also established the Colonial Penn Group ("CPG") in which he and his wife, also a Respondent here, became and remained principal shareholders. Thereafter, CPG itself began to underwrite health insurance for members of AARP and NRTA (hereinafter collectively referred to as the "Associations") (App. 78a).[2] The Associations endorsed and exclusively promoted CPG insurance and other products through Association publications, newsletters and local chapters. CPG utilized the non-profit mailing privileges of the Associations to solicit and expand its business (App. 4a, 78a-79a).

The court of appeals found that CPG occupied a unique position to assure itself of the Associations' insurance endorsement because "Davis and his companies managed the AARP and NRTA insurance plans" (App. 78a). The court of appeals also found that

> "The associations encouraged their members to purchase insurance, travel and other products and services exclusively through Davis-controlled entities, including insurance subsidiaries, group travel companies, and employment agencies. Davis' entities, moreover, had the exclusive right to advertise in the associations' publications and were permitted to do so at what appears to be substantially less than the fair market value of such advertising. CPG also maintained the membership lists of the associations in its computers." (App. 78a-79a).

The revenues and profits generated from Davis' domination and control of the Associations began to at-

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[2]By 1973, the value of the Davis' holdings in CPG were reported to be worth nearly $200 million. *Money* Magazine, (March 1975).

tract national attention by the mid-1970's. Thus, the court of appeals noted that:

> "As AARP and NRTA grew, so did Colonial Penn and its various subsidiaries, its total revenues being $171 million in 1972 and $445 million in 1976. The AARP/NRTA health insurance plans generated over $261 million in premiums in 1977. As of January 1, 1976, CPG led 929 major United States corporations in profitability with a five-year average annual return on capital of 33.5%, a figure nearly double the profitability of either IBM or Xerox and three times greater than the median return of 11.3% for the entire insurance industry. (App. 79a).

Notoriety and questions regarding Davis' involvement in the Associations also arose during this period.[3]

B. Commencement of Litigation in 1976.

In 1976, a companion action to the instant case was filed in state court in New York by Frieda Lederer against Davis, CPG and its Chairman, and AARP and its Executive Director, Harriet Miller (App. 79a). The complaint alleged breaches of fiduciary duty and violations of Section 340 of New York General Business law (known as the

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[3]In the March 1975 issue of *Money* magazine, the author noted that the Associations' membership had increased "tenfold" between 1966 and 1974. One stock analyst described Davis' selling of insurance through the Associations as "the best marketing thing I have ever seen." "A Word to the Wise About Old Age Groups," *Money* (March, 1975). *See also* "Health Insurance for Older People; Filling the Gap in Medicare," *Consumer Reports* (January, 1976); "Bedmates: Colonial Penn Group and the American Association of Retired Persons Have an Unusual Relationship: You Might Even Call It Incestuous," *Forbes* (February 1, 1976).

Donnelly Act). Although the suit was styled as a class action brought on behalf of AARP insurance-buying members, no damages were sought. Mrs. Lederer was the mother-in-law of class counsel Irving Malchman, a partner in the Kaufman, Taylor, Kimmel & Miller law firm ("Kaufman-Kimmel") which had filed the action.

When the firm of Shea, Gould, Casey & Clemenko (hereinafter "Shea & Gould") joined Kaufman-Kimmel as plaintiffs' counsel in 1977 and filed an amended state court complaint, Gerta C. Conway, who had been asked by her brother to join the suit, was substituted as the lead plaintiff (App. 79a).[4] The new action, also brought as a class action on behalf of insurance-buying AARP members, also alleged fraud, breach of fiduciary duties, and violation of state antitrust laws. Again, no damage relief was sought (App. 80a).

Later in 1977, Kaufman-Kimmel and Shea & Gould filed the present suit in the Southern District of New York alleging violations of Sections 1 and 2 of the Sherman Act (15 U.S.C. §§1, 2). The lead plaintiff was Nathan Malchman, brother of attorney Irving Malchman. Along with Irving Malchman's mother-in-law (Mrs. Lederer) and the sister of Milton Gould's chauffeur (Mrs. Conway), Nathan Malchman claimed to represent a class of two and one-half million insurance-buying AARP members. Except for briefing on issues raised by defendants' motion to dismiss. (which issues were never decided), the federal action remained dormant until the settlement in question was reached in 1980 (App. 80a-81a).

By 1979, Davis' and CPG's relationship with the Associations was under intense scrutiny in a number of quarters,

[4]Mrs. Conway's brother, Alvin Curley, was the chauffeur of Milton Gould, the senior and name partner in Shea & Gould.

including investigations by the United States Postal Service for alleged abuse of the Associations' non-profit mailing privileges and by the Securities and Exchange Commission. Reports critical of CPG had been issued by the Massachusetts and Wisconsin Insurance Commissions. In 1978, the Associations' Executive Director Harriet Miller publicly broke with Leonard Davis and attacked his and CPG's domination of the Associations (App. 7a, 80a).[5]

C. Questions Raised But Not Resolved Regarding Adequacy of Class Representatives.

As of early 1979 – even though the present case and its companion state court action had been pending for more than a year – plaintiffs had obtained no discovery from defendants (App. 80a). Instead, defendants had assumed the offensive in the litigation and were vigorously attacking in the state action the adequacy of the named-plaintiffs to represent the putative class in light of named-plaintiffs' familial relationships with counsel and allegations of champerty. (App. 80a). Defendants had moved to compel testimony from the named-plaintiffs, which then included William Deautriell and Louis Stone, relating to their relationships with their counsel and facts pertaining to solicitation of them to become plaintiffs. Inquiry into these matters was never concluded as to any plaintiff except Ms. Conway, on which the issue of solicitation was

[5]Highly acrimonious litigation ensued in the Superior Court in the District of Columbia, *Miller v. Davis*, Super. Ct. No. 4367-78 (Complaint reprinted in Court of Appeals' Appendix, pp. 654-72), which generated additional adverse publicity, including a nationwide broadcast on CBS' "Sixty Minutes" on May 14, 1978.

left in a confused and contradictory state.[6] Neither the state nor federal court ever determined in an adversarial environment the adequacy of these named-plaintiffs to represent any class; neither court passed upon whether this action was appropriately maintained as a class suit.[7]

D. The Stipulation of Settlement

In response to the critical scrutiny by the media and state and federal agencies, the Associations in early 1979 announced the adoption of several resolutions designed to establish their independence from Davis and CPG (App. 5a-6a).[8]

In 1980, CPG and the Associations agreed formally to terminate their relationship. A lengthy separation agreement was negotiated among the defendants and executed on September 1, 1980 (App. 81a). It provided for various payments to be made by CPG to the Associations, return of their membership lists, and competitive bidding for Association-endorsed insurance. (Court of Appeals Appendix, pp. 26-76).

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[6]Defendants agreed to waive further inquiry into these matters as part of an informal agreement to resolve several discovery disputes. No discovery was ever undertaken into the adequacy of Nathan Malchman to represent the class in the federal action.

[7]While a motion for class certification was filed it the state action, it was withdrawn.

[8]The Resolutions, in which neither plaintiffs nor their counsel had any involvement or participation in drafting or adopting, provided for termination of the Association's endorsements of CPG insurance and products; acceptance of advertising in Association publications; establishing Association custody of their membership records; elimination of the right of Davis to attend Association Board meetings; and exploration of discontinuance of CPG insurance (App. 5a-6a).

The terms of the November 1980 stipulation of settlement under review here, in the words of the court of appeals, "essentially incorporated the terms of the September 1980 voluntary agreement among the defendants." (App. 6a). The Court further found that "on the basis of chronology alone, it appears, to say the least, that the settlement adds very little to the benefits obtained for the plaintiffs as a result of the voluntary agreement reached in September 1980" (App. 20a).

According to counsel for the plaintiffs and the defendants, they engaged in settlement discussions of this action and the companion state court suit during two periods: in late 1978-early 1979 and in 1980 (App. 23a-24a). Attorneys fees for plaintiffs' counsel were discussed throughout the settlement negotiations (App.36a-40a). Defendants' counsel believed that plaintiffs were seeking approximately $4 million in fees at the outset of negotiations; counsel for CPG and the Associations suggested that they would agree not to oppose an award which did not exceed $1 million (App. 36a-37a & n.2). *Ultimately, and concededly before any written drafts of the substantive terms of the settlement were ever exchanged, defendants agreed not to oppose an award of costs and attorneys' fees which did not exceed $2.325 million* (App. 41a).

Defendants insisted – for settlement purposes only – and plaintiffs' counsel agreed to expand the class from 2.5 million insurance-buying ARRP members to include non-insurance-buying AARP members and insurance and non-insurance-buying members of NRTA and AIM, AARP's pre-senior citizen division. Although neither the state nor federal complaint sought damages, the settlement purported to extinguish any and all damage claims that the 11.2 million class members in the expanded class might have, including direct, derivative, compensatory

and punitive damages.[9] Rather than dismiss the federal suit, defendants also insisted that the proposed settlement be approved by the federal court to obtain the nationwide *res judicata* effect which such an order would provide.[10] Plaintiffs' counsel also acquiesced in this demand. The stipulation of settlement embodying these provisions and reiterating the terms of the defendants' September 1, 1980 separation agreement was executed on November 4, 1980.

E. Approval Proceedings in the State Court

The parties' stipulation of settlement contemplated the approval of both the New York state court and the United States District Court for the Southern District of New York. Both courts readily approved amendments to the complaints which expanded the class almost five-fold and tentatively granted class certification. At the request of the parties, the state court appointed a referee who conducted several meetings with counsel during which counsel acknowledged the simultaneous negotiation of attorneys fees and substantive issues.

Although the referee approved the settlement, the full amount of fees defendants agreed not to oppose, and a proposed class notice, the state court has not yet granted final approval to this settlement. Rather, the court has in-

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[9]A suit brought by two AARP members in California raising, in the words of CPG counsel, essentially the same issues as this litigation but seeking punitive damages from CPG was settled in March 1981 (four months after the instant settlement) for $500,000. *Copitka v. Colonial Penn Group, Inc.*, No. 44274 (Cal.Super.Ct. San Diego Cty. 1979) (App. 89a & n.3, 18a-19a).

[10]In 1980, the law was unsettled as to whether a state court order approving a class action settlement would be given extraterritorial *res judicata* effect.

formally stayed its proceedings regarding this settlement for more than three years while proceedings described hereafter have been ongoing in the federal courts.

F. Approval Proceedings in the Federal Courts.

The district court initially approved this settlement on September 10, 1982, without ever holding an evidentiary hearing or ever ruling upon the discovery requests filed by counsel for objectors.[11] Objectors promptly appealed, and on May 2, 1983, a unanimous panel of the Second Circuit reversed and remanded this case for development of a record, detailed findings, and analysis of several specific matters (App. C).[12]

On remand, objectors moved to compel responses to discovery requests which had been previously filed, and they again urged the district court to conduct an evidentiary hearing. The district court announced at the outset of the remand proceedings that it would approve the settlement regardless of the record developed or arguments made. Accordingly, the district court denied objectors the right to conduct any discovery,[13] refused to accept or

[11]The district court did not even file a memorandum or opinion addressing the hundreds of pages of arguments advanced by objectors. The court merely signed an order approving settlement proffered by class counsel.

[12]Although the court's earlier opinion had recited at least a dozen areas requiring further inquiry and analysis, the court of appeals in the instant decision — in a remarkable about-face — found that objectors had failed to raise cogent factual objections to the settlement (App. 8a).

[13]Without discovery, objectors filed a detailed Offer of Proof as to matters which discovery and a hearing would have developed. Counsel also filed an affidavit identifying materials in the state court record which were inadequate to support various factual findings required by the court of appeals' first decision.

review the state court record, ridiculed the need to examine the adequacy of named-plaintiffs' representation of the class, and declined to hold an evidentiary hearing. Approval of the settlement the second time formally occurred with the entry of a judgment on June 29, 1984.

The settlement approved by the district court provides no monetary recovery to the class even though it purports to extinguish damage claims with potential value well in excess of $100,000,000. The settlement essentially incorporates the steps defendants had previously agreed among themselves to perform to establish the independence of AARP and NRTA, but expands the class, for *settlement purposes only,* from 2.5 million persons to 11.2 million class members. Finally, in light of defendants' agreement not to oppose an award of fees and expenses to class counsel which did not exceed $2,325,000, the district court awarded the entire sum to class counsel.

As described above, the court of appeals, though sharply divided, nevertheless affirmed the district court's order with a single modification — reducing attorneys' fees for class counsel from $2,085,901 to $1,912,814 (App. 28a & n.8). In dissent, Judge Mansfield — using the district court's own findings as to the value of individual claims which had been negotiated away — found that "potential recovery" of damages here ranged from $40 to $80 million per year over a seven-year period (App. 35a). Reviewing the statements of defense counsel made before the state court referee, which are quoted at length in the dissent, Judge Mansfield observed:

> ". . . it is difficult *not* to conclude that plaintiffs' counsel were unwilling to give the class' damage claims of some $40-$80 million per year until they were firmly assured that there would be no

opposition to their proposed $2,325,000 in legal fees." (App. 41a). (Emphasis supplied).[14]

For the reasons set forth hereafter, the court of appeals' decision should be reviewed by this Court.

REASONS FOR GRANTING THE WRIT

This case presents several issues involving class actions which this Court has not previously addressed. This Court has granted certiorari in *Evans v. Jeff D.*, (No. 84-1288), which involves the propriety of defendants' insistence that class counsel waive any claim to fees. This case presents the mirror image of the issues involved in *Evans,* namely, whether class counsel can insist on negotiation of their fees simultaneously with negotiation of substantive issues affecting the class.

The threat posed here to legitimate use of the class action a device for "pool[ing] claims which would be uneconomical to litigate individually", *Phillips Petroleum Co. v. Shutts,* ____ U.S. ____, 105 S.Ct. 2965, 2974 (1985), is far more severe than that in *Evans.* The practice at issue in *Evans* will lessen the availability of counsel willing to undertake class suits where compensation depends on recovery of statutory fees. The abuses presented here pervert the class action and allow its use as a device for the mass preclusion of potentially valuable claims and for the enrichment of

[14]Class counsel's time sheets, which are in the record, corroborate this finding. Those logs show that class counsel recognized that they could use the threat of pursuing damage claims as leverage to obtain a huge fee award and that they actively began researching and drafting a damage complaint only *after* settlement negotiations began. (Time entries for Mr. Lesch, 2/13/79-2/19/79; Mr. Sutter, 2/16/79-2/20/79; M. Reston, June/July, 1979; Stanley Kaufman, 3/7/80-3/14/80; Fran Jacobs, 2/8/80-2/14/80; 4/8/80-4/9/80; 5/6/80-5/8/80).

counsel in derogation of the rights of absent class members. Each of the abuses at issue here independently violate due process and Rule 23. Cumulatively, they constitute an insidious corruption of the class action mechanism. This Court's review is necessary to assure that the interests of class counsel are not placed ahead of absent class members; that the class action does not become primarily a vehicle for claim preclusion rather than claim vindication; that absent class members be accorded the opportunity to explore and air questions regarding the fairness of proposed settlements and tainted settlement negotiations; and that federal courts carry out their responsibilities as guardians for the interests of absent class members rather than according rubber stamp approval to proposed settlements.

I. A CLASS ACTION SETTLEMENT CANNOT BE APPROVED CONSISTENT WITH THE DUE PROCESS CLAUSE WHEN CLASS COUNSEL NEGOTIATED AWAY VALUABLE DAMAGE CLAIMS IN RETURN FOR DEFENDANTS' AGREEMENT NOT TO OPPOSE A LARGE ATTORNEYS' FEE, WHERE THE NAMED-PLAINTIFFS HAVE FAMILIAL AND CLOSE PERSONAL RELATIONSHIPS WITH CLASS COUNSEL AND WHERE OBJECTORS TO THE SETTLEMENT HAVE BEEN DENIED ANY DISCOVERY AND AN EVIDENTIARY HEARING.

Only last Term, this Court commented upon the salutary purpose of class action litigation: "Modern plaintiff class actions . . . permit the plaintiffs to pool claims which would be uneconomical to litigate individually." *Phillips Petroleum Co. v. Shutts*, ____ U.S. ____, 105 S.Ct. 2965, 2974 (1985).[15] Class members, however, can be bound by

[15]As noted above, class counsel never sought damage recovery in the state or federal complaints they filed. Although counsels' time records show that they actively researched the recovery of damages

class action adjudications and settlements only if the litigation or settlement process "fairly insures the protection

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only after settlement negotiations began in an obvious attempt to assure recovery of their fees, see n. 14, *supra*, class counsel have asserted two reasons why they eschewed pursuit of damages. They have argued – alternatively – (1) that the cost of mailing the class notice would have been prohibitive; and (2) that damages for each class member were so small that when balanced against the cost of processing of such claims, the net recovery would have been virtually worthless. Both of these asserted reasons for failing to seek damages are wholly without merit.

In its 1983 decision, the Second Circuit rejected the first argument, noting that in cases involving fiduciary breaches, such as this, the costs of sending notice can properly be shifted to defendants (See *Eisen* v. *Carlisle & Jacquelin*, 417 U.S. 156, 178-79 & n. 15 (1974) citing *Dolgow v. Anderson*, 43 F.R.D. 472 (E.D. N.Y. 1968); *Sanders v. Levy*, 558 F.2d 636, 646 (2d Cir. 1976), *rev'd on other grounds, sub. nom., Oppenheimer Fund, Inc. v. Sanders*, 437 U.S. 340, 363 (1978) and/or that notice to the class printed in the Associations' publications at a modest cost could have been ordered as an alternative to a separate mailing (App. 94a-95a).

Counsel's second argument turns on the estimated value of the damages each class member could have recovered. The district court estimated that antitrust damages could be as large as $32.40 per year per class member (App. 58a). Since damages were recoverable for a seven-year period, each class member's damages could have exceeded $200. One of class counsel acknowledged that damages were likely to be less than $100 per class member (App. 57a). Even though the much smaller $100 figure translates into $250,000,000 in class-wide damages, the district court found that "[t]his is obviously a situation where the value of damage claims would be so small as to be virtually meaningless. . . ." (App. 58a). The district court's conclusion that class damage claims were "meaningless" ignores the very purpose of class adjudication, which is to litigate relatively small claims such as these. Indeed, in *Phillips Petroleum Co.*, Justice Rehnquist acknowledged that the claims there averaged "about $100 per plaintiff." He stated that "most of the plaintiffs would have no realistic day in court if a class action were not available." 105 S.Ct. at 2974. Plainly, the contention that class members' damage claims here were *de minimis* is totally at odds with both the potential recovery of more than a quarter-billion dollars and the purpose of class actions.

of the interests of absent parties who are to be bound by it." *Hansbery v. Lee,* 311 U.S. 32, 42 (1940). Adequacy of representation of absent class members' interests "at all times" is required by the Due Process Clause. *Phillips Petroleum Co. v. Shutts, supra,* 105 S.Ct. at 2975.

Although the requirement of adequate representation is often associated with a duty the class representative must discharge, it is not the duty of an individual alone "but a requirement that must be met by the process of class adjudication taken as a whole." *Developments in the Law-Class Actions,* 89 Harv.L.Rev. 1318, 1411 (1976).

Rule 23 of the Federal Rules of Civil Procedure incorporates these due process guarantees by requiring (1) as a "prerequisite" to class certification that "the representative parties will fairly and adequately protect the interests of the class" (subsection (a)(4)); (2) that the court determine whether class maintenance will be permitted (subsection (c)(1)); (3) careful supervision of class actions by such orders as the court deems "appropriate" (subsection (d)); and (4) that no class action be "dismissed or compromised without approval of the court" (subsection (e)).

To assure due process, the courts have held that class representatives cannot have any interests antagonistic to the interests of the class;[16] that, in controlling class actions and passing upon settlements, the courts must act as "guardians" of the rights of absentees;[17] that class counsel and

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[16] *Eisen v. Carlisle & Jacquelin,* 391 F.2d 555, 562-63 (2d Cir. 1968), *vacated and remanded on other grounds,* 417 U.S. 156 (1974).

[17] *Norman v. McKee,* 431 F.2d 769, 774 (9th Cir. 1970), *cert. denied sub nom. ISI Corp. v. Meyers,* 401 U.S. 912 (1971); *Girsh v. Jepson,* 521 F.2d 153, 157 (3d Cir. 1975). See also *Deposit Guaranty Nat'l Bank v. Roper,* 445 U.S. 326, 331 (1980) (district court has responsibility to protect absent class members).

the named-plaintiffs are impressed with fiduciary obligations with regard to absentee class members;[18] and that class counsel must assiduously avoid circumstances involving potential conflicts of interest with the class they are obligated to represent.[19]

A. The Entire Settlement is Tainted by Class Counsels' Fee Negotiations Which Were Conducted Before and During Discussions Regarding the Substantive Rights of the Class.

The negotiation of class counsel's fee is an area where obvious conflicts of interest may arise. The conflict here was neither a potential nor an imagined one. The dissenting opinion makes clear that counsel for the parties "acknowledged that they had agreed, long before the terms of the settlement had firmly been reached, that the $4.5 million attorney's fee limit originally sought by plaintiffs' counsel would be reduced to $2,325,000 and that this

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[18] *Greenfield v. Villager Industries, Inc.*, 483 F.2d 824, 832 (3d Cir. 1973); *Shelton v. Pargo, Inc.*, 582 F.2d 1298, 1305-06 (4th Cir. 1978); *Pettway v. American Cast Iron Pipe Co.*, 576 F.2d 1157, 1176-77 (5th Cir. 1978), *cert. denied*, 439 U.S. 1115 (1979). *See also Young v. Higbee Co.*, 324 U.S. 204, 213 (1945). ("[Parties] cannot avail themselves of the statutory privilege of litigating for the interest of a class and then shake off their self-assumed responsibilities to others by a simple announcement that henceforth they will trade in the rights of others for their own aggrandizement.")

[19] *Zylstra v. Safeway Stores, Inc.*, 578 F.2d 102, 104-05 (5th Cir. 1978); *Kramer v. Scientific Control Corp.*, 534 F.2d 1085, 1090-91 (3d Cir. 1976), *cert. denied*, 429 U.S. 830 (1976); *Bachman v. Pertschuk*, 437 F.Supp. 973, 976-77 (D.D.C. 1977); *Kahree v. Western Elec. Co.*, 82 F.R.D. 196, 199-200 (D.N.J. 1979). *See generally*, Note, *Conflicts in Class Actions and Protection of Absent Class Members*, 91 Yale L.J. 590 (1982).

figure would not be opposed by the defendants." (App. 40a-41a). Based on the foregoing, Judge Mansfield found that "it is difficult not to conclude that plaintiffs' counsel were unwilling to give [up] the class' damage claims of some $40-$80 million per year until they were firmly assured that there would be no opposition to their proposed $2,325,000 in legal fees." (App. 41a).

The courts and commentators have noted that any agreement by defendants to pay a definite amount of fees to class counsel "would present the potential for a collusive settlement. . . .", *Barnett v. Pritzker,* 73 F.R.D. 430, 432 (S.D.N.Y. 1977). Even where the amount of fees is not fixed, a plaintiffs' lawyer will have "a strong motive so as to conduct himself that defendants will not question or oppose the amount for which he ultimately applies . . . ." *City of Philadelphia v. Chas. Pfizer & Co.,* 345 F.Supp. 454, 471 (S.D.N.Y. 1972). Nor is the potential for conflict avoided where, as here, only injunctive relief is obtained:

> "In suits for injunctive relief . . . bargaining by the class attorney may give rise to a conflict of interest . . . [I]f a suit for injunctive relief is settled, the class attorneys' fee may depend upon the agreement of the class opponent, and the class attorney may be tempted to trade off class relief in order to secure compensation." *Developments in the Law - Class Actions,* 89 Harv.L.Rev. 1318, 1609-10 n. 132 (1976).

The only way to assure that such trade-offs do not occur is for the courts to insist that fee discussions be postponed until *after* all substantive issues affecting the class have been resolved. *Prandini v. National Tea Co.,* 557 F.2d 1015, 1020-21 (3d Cir. 1977); *Lyon v. Arizona,* 80 F.R.D. 665, 669 (D.Ariz. 1978).

Because the rights of absentee class members may be unfairly compromised through settlements, at least four circuits have expressed strong disapproval of simultaneous settlement negotiations involving attorneys' fees and merits issues which decisions are in conflict with the decision below. *Jeff D. v. Evans,* 743 F.2d 648, 651-52 (9th Cir. 1984), *cert. granted,* ____ U.S. ____, 105 S.Ct. 2319 (1985) (No. 84-1288); *Mendoza v. United States,* 623 F.2d 1338, 1352-53 (9th Cir. 1980), *cert. denied,* 450 U.S. 912 (1981); *Pradini v. National Tea Co.,* 557 F.2d 1015, 1020-21 (3d Cir. 1977); *Pettway v. American Cast Iron Pipe Co.,* 576 F.2d 1157, 1216 n. 71 (5th Cir. 1978), *cert. denied,* 439 U.S. 1115 (1979); *Obin v. Dist. 9, Int'l Ass'n of Machinists,* 651 F.2d 574, 582 (8th Cir. 1981).[20]

The issues presented here affect class action litigation far more directly and seriously than *Evans,* which this Court will review this Term. The danger posed in *Evans* is that conscientious class counsel, when forced to choose between their own interests in recovering fees and obtaining benefits for the class, will disclaim fees and thus undermine the strong federal policy of adequately compensating prevailing counsel in civil rights litigation. Class counsel who are forced to negotiate such settlements will, most likely, assure the greatest benefits for the absentee class members. Here, the issue is one of due process; it directly and substantially affects the rights of absent class members which may be, and here were, sacrified or traded for defendants' agreement not to oppose a large fee award.

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[20]In *Moore v. National Ass'n of Security Dealers,* 72 F.2d 1093 (D. C. Cir. 1985), the District of Columbia Circuit declined to award fees to class counsel where class counsel had voluntarily offered to waive any claim to fees which waiver was accepted by defendants and incorporated into the settlement.

The Second Circuit majority's approval of this settlement, in which fee issues were negotiated before settlement drafts embodying the substantive issues were even exchanged, is in sharp conflict with decisions from the four circuits cited above. This issue alone warrants review by this Court.[21]

B. The Due Process Rights of the Class Could Not be Fairly and Adequately Represented by Named-Plaintiffs Who are Relatives and Close Personal Friends of Class Counsel.

Although the proffered settlement provides no monetary benefits to the class while lavishly rewarding class counsel with more than $2,000,000 in fees and disbursements, the courts below swept aside the need for any serious inquiry into the adequacy of the named-plaintiffs

[21] Judge Oakes' reliance on the conclusory affidavits of counsel for the parties that they negotiated fees only after a "framework" of settlement had been agreed upon overlooks that fact that at least 26 substantive issues remained to be negotiated after the first settlement drafts were exchanged in August 1980. These 26 areas were set out in a Sept. 15, 1980 letter by defense counsel to class counsel in order "to expedite the course of our *negotiations* . . . of the stipulation of settlement." (Letter of Michael Oberman to Michael Lesch, Sept. 15, 1980). Moreover, the Court's reliance upon counsel's representations belies the vigilance which the courts — as guardians of absent class members — must exercise in evaluating such statements "since it has been shown that there may be a bias toward 'settlements in which the attorney for the class agrees to trade off a smaller total award payment by the defendant for a larger fee.' " 7A C. Wright, A. Miller & M. Kane, *Federal Practice & Procedure*, § 1797 at p. 231 (1985 Supp.), quoting *Mandujano v. Basic Vegetable Prods., Inc.*, 541 F.2d 832, (9th Cir. 1976). Here, of course, counsel traded away all of the class' damages in return for a truly enormous fee; and even the "majority" acknowledged that on "first impression" it appears that "the negotiations leading to the stipulation of settlement amounted to little more than a trade of damages relief foreclosure for attorneys' fees." (App. 20a).

to represent the class.[22] By contrast, Circuit Judge Mansfield noted that several of the plaintiffs had relationships with counsel which placed them in a clearly antagonistic position vis-a-vis absentee class members:

> "The lead plaintiff, Nathan Malchman (whose deposition was never taken), is the brother of Irving Malchman, legal counsel for the class. One of the original named plaintiffs, Frieda Lederer, was Irving Malchman's mother-in-law. Greta Conway is the sister of the chauffeur for class counsel. Louis Stone is a personal friend of class counsel. *All of this raises the question of whether, absent these close relationships, the named plaintiffs would not, because of their desire to see their relative or friend receive a generous share of the $2,325,000 legal fee, be much more willing to give up their potential recoveries than would the other eleven million plus members of the class who have no such relationships with class counsel.*" (App. 41a-42a). (Emphasis supplied).

The majority's approval of class counsel's brother, the sister of the chauffeur to class counsel and the close friend and dining companion of another of the plaintiffs' counsel to serve as class representatives constitutes a mockery of the "adequacy" requirement and is directly at odds with no less than three other circuit decisions. *Susman v. Lincoln Am. Corp.*, 561 F.2d 86 (7th Cir. 1977); *Turoff v. May*

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[22] Judge Oakes went outside the record to examine the depositons of a few of the named-plaintiffs, but he failed to note that defendants' inquiries into solicitation and relationships with counsel were, in all but one instances, never pursued. Finally, despite objectors' recitation in their Reply Brief of numerous areas of inquiry they would have pursued, Judge Oakes incorrectly stated that objectors had not identified questions they would have posed to the named plaintiffs (App. 12a).

Co., 531 F.2d 1356 (6th Cir. 1976);*Shroder v. Suburban Coastal Corp.*, 729 F.2d 1371 (11th Cir. 1984). This issue, independent of the others described herein, should be reviewed to resolve the circuit conflict as to whether family members and close personal friends of class counsel should be disqualified from serving as class representatives.

C. The Refusal to Permit Discovery and Failure to Conduct an Evidentiary Hearing into the Circumstances Surrounding and Fairness of the Proffered Settlement Violated the Due Process Rights of Absentee Class Members.

The right to a hearing is the essence of due process. *Boddie v. Connecticut,* 401 U.S. 371, 377-79 (1971); *Board of Regents v. Roth,* 408 U.S. 564, 569-72 (1972); *Wolff v. McDonnell,* 418 U.S. 539, 557-58 (1974), citing *Joint Anti-Fascist Refugee Comm. v. McGrath,* 341 U.S. 123, 168 (1951) (Frankfurter, J., concurring); *Dougherty v. Harper's Magazine Co.*, 537 F.2d 758, 761 (3d Cir. 1976). The right to a meaningful hearing necessarily includes the right to conduct discovery or otherwise obtain evidence. Even Judge Oakes found that "[o]n first impression the district court's denial of discovery appears in conflict with the spirit of our remand." (App. 9a). He further stated that that "initial impression" "seems difficult to avoid" with regard to the adequacy of representation provided by the named plaintiffs. (App. 9a). The majority nevertheless – in marked contrast with the court's earlier decision requiring a more detailed inquiry and analysis into more than a dozen different areas raised by objectors – concluded that neither discovery nor an evidentiary hearing were required here because objectors had failed to advance cogent

factual reasons why the settlement should be rejected (App. 8a).

Because objectors to a settlement will be bound by its terms, it has been held that they are entitled to conduct discovery into the manner in which settlement negotiations were conducted, *In re General Motors Corp. Engine Interchange Litigation,* 594 F.2d 1106, 1131 (7th Cir. 1979), *cert. denied,* 444 U.S. 870 (1979), and otherwise "to test . . . the strengths and weaknesses of the proposed settlement," *Girsh v. Jepson, supra,* 521 F.2d at 157. Objectors are also entitled to participate in a hearing on the adequacy of the settlement, to submit evidence and to cross-examine witnesses. *Flinn v. FMC Corp.,* 528 F.2d 1169, 1173 (4th Cir. 1975), *cert. denied,* 424 U.S. 967 (1976); *Greenfield v. Villager Industries Inc., supra,* 483 F.2d at 833; *Cohen v. Young,* 127 F.2d 721, 724 (6th Cir. 1942), *cert. denied,* 321 U.S. 778 (1944).

These essential due process guarantees were not provided to objectors here. Review by this Court is essential to assure that the rights of absentee class members are fully protected and consistent with the requirements of the Due Process Clause.

II. TENTATIVE CERTIFICATION FOR SETTLEMENT PURPOSES OF A CLASS NEARLY FIVE TIMES LARGER AND INVOLVING PERSONS PLAINTIFFS NEVER SOUGHT TO REPRESENT CONSTITUTES A PATENT ABUSE OF THE CLASS ACTION DEVICE.

The framers of Rule 23 contemplated that a determination as to whether a class action would be maintainable would occur "[a]s soon as practicable after the commencement of an action . . . ." and would occur in an adversarial

environment after an appropriate hearing. Rule 23 also provides that class actions cannot be "dismissed or compromised without approval of the Court . . . ," which should ordinarily occur after class status has been formally granted. Here, no motion for certification was ever filed in this action before the settlement was negotiated and submitted for approval. In the stipulation of settlement, defendants agreed to class certification for settlement purposes only of a class vastly larger than the 2.5 million persons plaintiffs claimed to represent in their complaint, which class purportedly included non-insurance buyers of AARP (whose claims are essentially derivative and in conflict with insurance buyers)[23] as well as members of NRTA and AIM, in which none of plaintiffs were members.[24]

Tentative class certification for settlement purposes has been vigorously condemned by the *Manual for Complex Litigation* §1.46, and has been the source of considerable controversy. *See In re Beef Industry Antitrust Litigation,* 607 F.2d 167, 173-78 (5th Cir. 1979), *cert. denied,* 452 U.S. 905 (1981). The distinguished Board of Editors, on behalf of the Federal Judicial Center, have articulated in

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[23]Several cases have held that plaintiffs whose damage claims are primarily derivative cannot serve as representatives of a class whose damage claims are direct. *Ruggiero v. American Bioculture, Inc.,* 56 F.R.D. 93, 95 (S.D.N.Y. 1972); *Hawk Indus., Inc. v. Bausch & Lomb, Inc.,* 59 F.R.D. 619, 624 (S.D.N.Y. 1973); *Petersen v. Federated Dev. Co.,* 416 F.Supp. 466, 475, n. 6 (S.D.N.Y. 1976); *Schnorbach v. Fuqua,* 70 F.R.D. 424, 428-30 (S.D.Ga. 1975).

[24]Objectors' challenges to the constitutional standing of the named-plaintiffs to represent members of other Associations and non-insurance buying AARP members were matters about which the Second Circuit expressed concern during the first appeal (App. 90a) citing, *Schlesinger v. Reservists Committee to Stop the War,* 418 U.S. 208, 216 (1974), but were not seriously addressed in the Second Circuit's most recent decision.

the *Manual* nine reasons why tentative class certification for settlement purposes should ordinarily not be granted:

> (1) Rule 23 does not expressly authorize formation of tentative classes for the purpose of settlement.
>
> (2) *There usually can be no assurance that the class members will be adequately represented in the settlement negotiations* until the court makes the findings, which are a condition precedent to the formation of a class, after an opportunity for an evidentiary hearing. Formation of a tentative class for the purpose of settlement, with a requirement that the class members accept the settlement or opt out and litigate independently, might deny the members of the class the opportunity to show the inadequacy of the representation of the class by the representative party or parties agreeing to the settlement and their counsel.
>
> (3) The *appropriate membership* of the class and the identity of the members ordinarily *should not be determined in the absence of an opportunity for hearing* and judicial findings of fact and conclusions of law. *Nor can there* usually *be any assurance that the tentative class will be composed of members without conflicting interests.* Absent such findings and conclusions, it may be difficult to determine how many members there are in a class, who they are, the aggregate of claims of all members of the class, the amount of the individual claim of each member in relation to the total claims of all members of the class and, therefore, the amount of money that will be payable to each member of the class. This information would seem to be essential for a member to

make any rational choice between whether to remain in the class and accept the benefits of the settlement or to opt out.

(4) If the *information relevant to liability, damages, and the expense of preparation for trial and of trial is not developed,* there usually cannot be a fair recognition in settlement negotiations of the potential liability of the party or parties opposing the class and the potential damages that might be recovered for the class.

(5) Formation of a tentative class for the purpose of settlement *preempts determination of the question whether the claim for relief should be litigated* for the members of the class or should be the subject of further pretrial preparation, with a view toward securing a better settlement or a trial on the merits. *It also preempts the question of which parties and counsel should represent the tentative class,* since there must be an unofficially negotiated earlier settlement for the purpose of the formation of the tentative class.

(6) The *formation* of a tentative class for the purpose of settlement *denies the class member the choice,* contemplated by amended Rule 23, *to become a member of the proposed class for the purpose of litigation,* with adequate representation as a member of the litigating class.

(7) Formation of such a class *denies a member of the class the right to appear in the action as a party* and to maintain the position of a litigating party.

(8) Formation of such a class might lead to a long delay in preparing the case for trial, for those parties who desire to litigate their claims for relief.

> (9) *In the absence of reasonable discovery conducted on an adversary basis by counsel representing the class, it is difficult to determine whether the proposed settlement has any relation to the economic facts of life relevant to the case.*

Manual For Complex Litigation, §1.46 (rev. ed. 1981) (Emphasis supplied). Each of these reasons and especially the ninth reason apply with particular force to this case. While several cases have approved settlements where tentative settlement classes have been agreed upon, *see* cases cited in *Beef Industry, supra,* 607 F.2d at 175-76 & n. 5, it has been held that courts should be "doubly careful" to assure that the settlement is otherwise proper and fair. *Ace Heating & Plumbing Co., Inc. v. Crane Co.,* 453 F.2d 30, 33 (3rd Cir. 1971); *Plummer v. Chemical Bank,* 668 F.2d 654, 657 (2nd Cir. 1982). Apart from the present case, no other decision has held that the plaintiff class can be expanded by a significant multiple not for recovery purposes but *solely to extinguish the claims of the class.* The magnitude of this abuse — affecting some 9,000,000 elderly Americans for whom this action was neither brought nor prosecuted — urgently requires this Court's review and correction.

CONCLUSION

This case involves a wide range of abuses of class actions which this Court has not previously considered. Several of the issues presented have resulted in decisions by the courts of appeals which are irreconcilable with the decision below. These issues clearly merit review and resolution by this Court. Accordingly, for the reasons set forth herein, Petitioners respectfully pray that certiorari be granted to review the decision of the Second Circuit.

Respectfully submitted,

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September 17, 1985

APPENDIX A

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

Nos. 434, 576 — August Term, 1984

(Argued: December 3, 1984 Decided: May 10, 1985)

Docket Nos. 84-7589, 84-7669

NATHAN MALCHMAN, GERTA CONWAY, WILLIAM DEAUTRIELL and LOUIS STONE,

Plaintiffs-Appellees,

v.

LEONARD DAVIS, SOPHIE DAVIS, COLONIAL PENN GROUP, INC., COLONIAL PENN FRANKLIN INSURANCE COMPANY, INTRAMERICA LIFE INSURANCE COMPANY, NATIONAL ASSOCIATION PLANS, INC., AMERICAN ASSOCIATION OF RETIRED PERSONS, NATIONAL RETIRED TEACHERS ASSOCIATION, CARRIE B. ALLEN, ORANDA BANGSBERG, BERNARD BERGGREN, JUNE BIGGAR, ARTHUR BOUTON, OLAF KAASA, CLARA L. KLEWENO, FLOYD E. TUMBLESON, J. LEONARD JOHNSON, C. E. CARMICHAEL, AMERICAN ASSOCIATION OF RETIRED PERSONS INSURANCE TRUST, DOROTHY M. CRIPPEN, JAMES J. BROWNING, LLOYD I. SINGER, CYRIL F. BRICKFIELD and JOHN J. MACWILLIAMS,

Defendants-Appellees,

MOUNTAIN PLAINS CONGRESS OF SENIOR ORGANIZATIONS, MR. & MRS. HUGH A. GROVES, FRANCIS SEELY, ESTELLE WHITTLE, HENRY WHITTLE, MR. & MRS. BURTON W. ATKINSON, MR. & MRS. C. E. DIETRICH, HARRIET MILLER, and ALICE VAN LANDINGHAM,

Objectors-Appellants.

Before:

MANSFIELD, OAKES and NEWMAN, *Circuit Judges.*

Appeal from a judgment of the United States District Court for the Southern District of New York, Thomas P. Griesa, *Judge*, approving the settlement of a class action asserting federal antitrust violations and approving an award of attorneys' fees and costs to plaintiffs.

Approval of settlement affirmed as modified. Judge Newman concurs in a separate opinion; Judge Mansfield dissents in a separate opinion.

Michael Lesch, New York, NY (Fran M. Jacobs, Shea & Gould, New York, NY, Stanley L. Kaufman, Irving Malchman, Kaufman Malchman & Kirby, New York, NY, of counsel), *for Plaintiffs-Appellees.*

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Geoffrey M. Kalmus, New York, NY (Michael S. Oberman, Kramer, Levin, Nessen, Kamin & Frankel, New York, NY, of counsel), *for the Association Defendants-Appellees.*

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OAKES, *Circuit Judge*:

This approval of an antitrust class action settlement comes before us a second time. In *Malchman* v. *Davis*, 706 F.2d 426 (2d Cir. 1983), we remanded approval of the settlement for further analysis of the adequacy of class representation and the adequacy, fairness, and reasonableness of the settlement itself—the latter with particular concern for the proposed award of attorneys' fees and costs in the amount of $2.325 million. Remand was ordered with the understanding that, while we were calling for "further analysis," we were not making "any attempt to circumscribe the permissible conclusions that the District Judge may reach upon completing his further consideration of the matter." *Id.* at 436 (Newman, J., concurring). On such further consideration, the district judge again concluded that the representation of the plaintiff class was adequate and the settlement, including attorneys' fees, was adequate, fair, and reasonable. *Malchman* v. *Davis*, 588 F. Supp. 1047 (S.D.N.Y. 1984). We affirm. Familiarity with the opinion of this court on the prior appeal and the opinion of the district court after remand will be assumed, though we will briefly restate the case to illuminate what follows.

This litigation and a companion state court action, *Conway* v. *Davis*, No. 10535/76 (N.Y. Sup. Ct. filed May

4, 1976), principally arise from the relationship between insurance companies created and controlled by Leonard Davis and two nonprofit retiree associations, the National Retired Teachers Association (NRTA) and the American Association of Retired Persons (AARP) (collectively the Associations). Some twenty years ago, Mr. Davis, an insurance broker, formed the companies that became Colonial Penn Group (CPG), an underwriter of group health insurance plans. From the 1960's until 1980, CPG became the first insurance company, and remained the only one, to underwrite health insurance policies for the members of the Associations. It also had the exclusive right to advertise in the Associations' publications, and, inter alia, maintained the membership lists of the Associations in its computers. The Associations in turn encouraged their members to purchase a variety of insurance products and services through CPG entities. Over twenty years of cooperation and mutual assistance between CPG and the Associations, together with numerous demographic factors, resulted in tremendous growth in the membership of the Associations and in CPG's profits. *See* 706 F.2d at 428. The arrangement had had many benefits to the parties even if it was a locked-in one.

In 1976, litigation commenced in state court in the form of a class action brought by Frieda Lederer on behalf of the class of insurance-buying members of the AARP, charging Davis, CPG, and others with fraud and breach of fiduciary duty and alleging, inter alia, that the class was overcharged for insurance policies purchased from CPG. A federal class action alleging antitrust liability was subsequently brought in October 1977, the class again consisting of the insurance-buying members of the AARP. Neither the state court nor the federal court action sought damages; rather, each sought injunctive re-

lief to terminate the relationship between Leonard Davis and CPG, on the one hand, and the Associations, on the other. The district court's opinion on remand now informs us that discovery was begun and basically continued in the state court action—in which there was no dispute concerning the jurisdiction of the court over the fraud and breach of fiduciary duty claims—with the understanding that the state court discovery would or could be used in the federal court action. We are also advised that, in response to mutual document requests, plaintiffs produced over 4,000 pages of documents and defendants over 100,000 pages of documents, of which plaintiffs made copies of over 65,000 pages. 588 F. Supp. at 1049-50 & n.1. Depositions were also taken by both plaintiffs and defendants from January 1979 through mid-May 1980, with some 66 days of testimony resulting in 11,850 pages of transcript and "numerous disputes during the discovery resulting in applications to the state court." *Id.* at 1050. Meanwhile, defendants filed a motion to dismiss the federal complaint, claiming that the action was barred by section 2(b) of the McCarran-Ferguson Act, 15 U.S.C. § 1012(b) (1982) (concerning applicability of the Sherman Act, Clayton Act, and Federal Trade Commission Act to insurance business), and that the plaintiffs lacked standing. This motion was never decided, despite the quantity of material submitted to the court, because by the spring of 1980 serious settlement negotiations were taking place, and by mid-June of 1980 the parties had requested the federal court to withhold decision. *Id.*

Meanwhile, in February 1979, the Associations had passed a series of resolutions—in essence, to discontinue their endorsement of certain CPG products other than group health insurance, to accept general advertising, to study other insurance programs, to negotiate with CPG

relative to membership maintenance and processing, and to consider the possibility of phasing out the Associations' group health insurance program (run by CPG). On September 1, 1980, the Associations signed an agreement with CPG, the substance of which is set forth in our previous opinion, 706 F.2d at 429. The agreement essentially provided for a termination of the relationship between the Associations and CPG as well as elimination of CPG's control over the Associations' membership lists and exclusive right to advertise in Association publications. The agreement also provided for payment of some $6.86 million from CPG to the Associations, and an agreement by CPG to spend an additional $4.5 million to promote membership in the Associations between January 1, 1980, and June 30, 1981. On November 6, 1980, the parties in the federal and state actions stipulated to a proposed settlement, which essentially incorporated the terms of the September 1980 voluntary agreement among the defendants. The proposed settlement did, however, add certain terms regarding (1) competitive bidding procedures for the placement of insurance by the Associations; (2) termination of the state and federal actions; (3) broadening of the plaintiff class to include all persons who were members of the Associations as of November 1, 1980, thereby increasing the class membership to over 11,000,000 persons; (4) class notification of the settlement and state court hearing through the Associations' news bulletins and magazines; (5) attorneys' fees, as will be set forth below; and (6) an escape clause for the defendants in the event that more than 10,000 class members were to opt out or if the settlement were disapproved by either the state supreme or federal district court or upon any appeal from either of such courts. *See id.* at 429-30. The district court now advises us, 588 F. Supp. at 1052, that 2,850

persons have opted out of the class while 11 have objected to the settlement.

The appellants objecting to the settlement are the same persons who previously objected—including Harriet Miller, the former executive director of the Associations, who played an instrumental role in bringing about the disassociation of CPG and the Associations, as well as the Mountain Plains Congress of Senior Organizations. They now urge that the district court erred and violated this court's mandate by granting renewed approval to the proposed settlement without allowing discovery and without conducting an evidentiary hearing. They contend that the settlement does not fall within a range of fairness reflecting adequacy of representation and that the district court made errors of law as well as incorrect assumptions regarding matters of fact. They object to approval of the attorneys' fees and conclude generally that the proposed settlement is contrary to the interests of the class, being "all cost and no benefit."

DISCUSSION

We begin with appellants' procedural objections. Their point is that the district court granted approval on remand without allowing discovery and without conducting an evidentiary hearing. Our prior opinion referred to the fact that the district court had "stated conclusions but made no specific findings" and that we could not properly review the settlement "because we do not have sufficient analysis of several pivotal issues." 706 F.2d at 427. We said that we could not "intelligently review the settlement on this record," *id.* at 433, and that while the district judge was entitled to rely on pertinent portions of the state court referee's report as

to reasonableness, "his reliance could not substitute for federal court inquiry as to matters pertinent to the federal suit that were either not considered or inadequately considered by the referee." *Id.* at 434. Judge Newman, concurring, supported "our call for further analysis." *Id.* at 436.

At the same time, we said that we did not expect a district judge to "convert settlement hearings into mini-trials on the merits," *id.* at 433, and that no further evidentiary hearing would be necessary unless the objectors raised "cogent factual objections to the settlement," *id.* at 434 (quoting *Weinberger* v. *Kendrick*, 698 F.2d 61, 79 (2d Cir. 1982), *cert. denied*, 104 S. Ct. 77 (1983)); *see also City of Detroit* v. *Grinnell Corp.*, 495 F.2d 448, 464 (2d Cir. 1974) (*Grinnell I*) (objectors must make "clear and specific showing that vital material was ignored by the District Court"). Thus we did not require that the district court open the case for further discovery and an evidentiary hearing unless the district court found that the objectors raised "cogent factual objections to the settlement." Whether such objections were raised can only be determined by reviewing the individual issues on which we asked for further analysis.

1. *Adequacy of class representation.* The first issue remanded for findings is whether the named plaintiffs were fair and adequate representatives for both the class of insurance buyers they purported to represent at the time suit was brought and the broadened class ultimately approved by the district court. Fed. R. Civ. P. 23(a)(4). In the district court, the objectors sought discovery as to "[t]he relationships of named-plaintiffs to counsel, and other information bearing upon adequacy of their representation of absentee class members." Discovery was

denied by the district court, which instead proceeded on the theory, citing *Fischer* v. *ITT,* 72 F.R.D. 170, 173 (E.D.N.Y. 1976), that "the 'touchstone' for denial of class action status was the question of whether the plaintiff had an interest in the attorney's fee," and that as "a matter of common experience in class actions," it is the attorneys and not the class plaintiffs "who make the litigation decisions, determine strategy, and negotiate settlement terms." 588 F. Supp. at 1057-58. The district court, attesting to "the high professional character of [plaintiffs' attorneys'] work," found that the class was represented by attorneys who had "acted with outstanding vigor and dedication." *Id.* at 1058.

On first impression, the district court's denial of discovery appears in conflict with the spirit of our remand, where we pointed out that "[a] judge has an obligation to consider whether the interests of the class are adequately represented" and that he or she "must examine the quality of representation with particular care where, as here, a class is sought to be broadly expanded after the litigation has been in process and for purposes of settlement." 706 F.2d at 433. Moreover, in this case an initial impression of impropriety in regard to class representation seems difficult to avoid; as we also pointed out, plaintiff Malchman is the brother of class counsel; plaintiff Conway is the sister of the chauffeur of class counsel; plaintiff Lederer was the mother-in-law of class counsel; and plaintiff Stone is a personal friend of class counsel. *Id.* at 432.

It appears now, however, that before settlement negotiations began, defendants had deposed the named plaintiffs at length on issues that included the ties between the named plaintiffs and class counsel; plaintiff Deutriell

had been deposed for three days, resulting in 611 pages of transcript; plaintiff Louis Stone had also been deposed for three days, resulting in 399 pages of transcript; plaintiff Conway had been deposed for three days, resulting in 380 pages of transcript; and Joseph Stone, a plaintiff in the state court (but not the federal court) action, had been deposed at comparable length on two days. Our perusal of these depositions, transcripts of which were handed to us at argument, demonstrates to us that the defendants' questioning of plaintiffs was searching, strenuous, and conducted at arm's length—as evidenced by the acerbic interchanges among the parties' counsel and the deponents.

Joseph Stone, a man of impressive credentials,[1] was, if anything, a fiercely independent plaintiff. After reading articles about group health insurance in Consumer Reports and Forbes Magazine, an article about Leonard Davis in the Washington Post, and a "Sixty Minutes" transcript on CPG and the Associations, he formed the impression that Leonard Davis handpicked the members of the Associations' board. At one point, while under examination by counsel for CPG and Leonard Davis, he suggested to counsel "that you do not become antagonistic. You do not raise your voice to me at any time. Witnesses, like everybody else, have rights, and I will not tolerate any nonsense on your part. You just ask the questions and I will answer them."

Plaintiff Deautriell apparently had learned about the Lederer case from objector Harriet Miller, whom he had

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[1] Mr. Stone is a lawyer and sometime consumer advocate who formerly served as Assistant District Attorney in New York County, Chief of the Criminal Court Bureau of that office and Judge of the Criminal Court of the City of New York.

called in reference to the Washington Post article. Deautriell was to obtain from the Lederers what was then the name of co-counsel for plaintiffs, Kaufman, Taylor, Kimmel & Miller (now Kaufman Malchman & Kirby). He became a plaintiff after learning for himself about the nature of the suit; there is no indication that he was solicited in any manner, shape or form.

Plaintiff Louis Stone wrote an investment letter for the firm then known as Shearson, Hayden & Stone, for whom he was a registered representative and vice president. According to Stone's deposition, in June 1978, Stone had lunch with his friend, Stanley L. Kaufman, counsel for plaintiff Lederer. Following the luncheon, over which the litigation was discussed, Stone volunteered to become a plaintiff "as a representative policy holder and as a social-minded participant in so-called benefits of this hospitalization plan for older people . . . in an inflating society who are subject to the hazards of sickness and old age without adequate incomes currently." Stone testified without hesitation that it was he who first raised the subject of his becoming a plaintiff. He, too, had some feisty words for defendants' counsel: "The objective here, it seems to me, is not to ascertain the truth of the facts, the objective is to discredit me as a plaintiff or as a witness and I wish you would state this objective and, of course, you don't." As he went on to say, "[a]nd although I don't hold myself out as one of nature's noblemen, I think that I have a duty as a citizen to help in the prosecution of evil."

Plaintiff Conway has worked full- and part-time for Social Concern Housekeeping Vendor Agency for some six years. Her late brother, Alvin Curley, had been a chauffeur for Milton Gould, of what was then Shea,

Gould, Climenko & Casey (now Shea & Gould), and had "overheard a conversation that Shea Gould was involved in a lawsuit against AARP and Colonial Penn." Her brother asked her if she wanted to join in. After that conversation, she received a call from one of the Shea, Gould lawyers, but she testified unequivocally that no lawyer had asked her to become a plaintiff in this action.

Appellants argue that the district court did not make an independent examination of the relationship between counsel and the named plaintiffs. While we think the district court's treatment of the adequacy of representation was somewhat limited, *cf. Susman* v. *Lincoln American Corp.*, 561 F.2d 86, 90-94 (7th Cir. 1977) (setting forth extensive analysis of adequacy of representation problems where named plaintiff related to plaintiff's counsel), our examination of the depositions indicates that the plaintiffs—particularly Joseph Stone, a plaintiff in the state court proceeding—were quite appropriate, perhaps even zealous members of the class. Moreover, as the brief of the plaintiffs-appellees points out, appellants failed to specify a single question that would have improved upon the defendants' searching depositions of the plaintiffs. Certainly in respect to the dual issues of representation and solicitation, appellants have furnished no "cogent factual objections" indicating the need for discovery or possible evidentiary hearing. *See Weinberger*, 698 F.2d at 79.

In the end, the question whether named plaintiffs are adequate class representatives is one committed to the sound discretion of the district court.[2] *See Ingram* v.

[2] It is because of, not despite, our belief in deference to the discretion of the district court that we have referred to the record in explanation of the district court's finding that class representa-

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Madison Square Center, Inc., 709 F.2d 807, 811 (2d Cir.), *cert. denied*, 104 S. Ct. 346 (1983); *Brick* v. *CPC International, Inc.*, 547 F.2d 185, 187 (2d Cir. 1976). Moreover, there is nothing to indicate, as the district court demonstrated, 588 F. Supp. at 1058, that expanding the originally defined class to include all AARP members, including those who had not purchased CPG insurance, and all members of NRTA and of Action for an Independent Maturity (AIM), a division of AARP, somehow made the original plaintiffs incapable of representing the class. To be sure, the class was apparently expanded to give defendants maximum protection against further litigation. But the district court found this to be a reasonable objective. *Id.* Furthermore, the interests of the members of AARP who purchased insurance are not antagonistic to the interests of the AARP members who have not purchased insurance, since all benefited from having the opportunity to purchase insurance from a carrier selected by competitive bidding as well as from the reorganization of the Associations' structure—the reform of advertising policy, the separation from CPG, and the termination of the Associations' promotion of CPG's non-health insurance projects. In short, the interests of the members of the broadened class in the settlement agreement were commonly held, and there is therefore no basis for disturbing the district court's finding on adequacy of representation.

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tion was adequate, given the district court's rather sketchy treatment of client-counsel relations that many, at first glance, would find suspect. *Cf. Susman*, 561 F.2d at 93 (noting that "the notion that the appearance of conduct is as important as the conduct itself is a predicate for the Code of Professional Responsibility").

2. *Adequacy, fairness, and reasonableness of the settlement.* The second major issue is the adequacy, fairness, and reasonableness of the settlement. *See, e.g., Weinberger*, 698 F.2d at 73; *Plummer* v. *Chemical Bank*, 668 F.2d 654, 659 (2d Cir. 1982). We have gained much from the district court's opinion, as well as from the briefs and record furnished to us on this appeal, and may now compare the substantive terms of the settlement to the likely result of a trial, *Protective Committee for Independent Stockholders of TMT Trailer Ferry, Inc.* v. *Anderson*, 390 U.S. 414, 424-25 (1968); *accord In re Traffic Executive Association-Eastern Railroads*, 627 F.2d 631, 633 (2d Cir. 1980), and examine the negotiating process for evidence of coercion or collusion. *Weinberger*, 698 F.2d at 74; *Robertson* v. *National Basketball Association*, 556 F.2d 682, 684 n.1 (2d Cir. 1977); *Grinnell I*, 495 F.2d at 465.

On comparing the possible results of a trial to the terms of the settlement, the key issue from a federal-court point of view is, as it always has been, the viability of a claim for damages by the plaintiff class under the antitrust laws. No such claim was made; our question on the previous appeal was whether one should have been, 706 F.2d at 435. We note at the outset that the principal question does not, perhaps, concern liability itself but rather remedy. We say this, because the prospect of liability under federal antitrust law was at least a factor in inducing defendants to acquiesce in what amounts to substantial injunctive relief *in exchange* for the foreclosure to class members of claims for relief in damages. We say "perhaps," however, because the McCarron-Ferguson defense, *see supra* at 3747, was still outstanding at the time of settlement. But the main question concerns the role that a potential claim for damages relief did play

or should have played in the litigation strategy of class counsel.

As the district court correctly observed, in order to obtain relief in damages, class members must prove "injury in fact," *see J.T. Gibbons, Inc.* v. *Crawford Fitting Co.*, 704 F.2d 787, 791-92 (5th Cir. 1983), by way of demonstrating that the insurance purchased from the defendant insurance companies either cost more or was of less value than insurance otherwise available to them absent the alleged anticompetitive activity. Even though the aggregated damages, as appellants point out, might be enormous, establishing individual damages would very likely require numerous subclasses. This is true since there were some seventeen different AARP plans and nine NRTA plans in effect during the relevant period from 1973 to 1980, 588 F. Supp. at 1054, and a method would have been required to compare the particular mix of premiums and benefits in each plan with the premiums and benefits that a claimant hypothetically would have paid or received in the absence of alleged antitrust violations. Our previous opinion noted that "means may be available to assess the harm to the class even if proof of each plaintiff's damages would be difficult," 706 F.2d at 435, and the district court apparently misinterpreted this to suggest, contrary to *Eisen* v. *Carlisle & Jacquelin*, 479 F.2d 1005, 1017 (2d Cir. 1973), *vacated and remanded*, 417 U.S. 156 (1974), that the claims of the various subclasses could be treated collectively as the claim of "the class as a whole." *Eisen*, 479 F.2d at 1014, 1018; *accord In re Hotel Telephone Charges*, 500 F.2d 86, 90 (9th Cir. 1974). What we referred to as "means" were computer programs that would simplify the proof of damages of subclasses. But apparently suggestions as to these were not forthcoming from the objectors on remand—not in

their "offer of proof," made when it was evident that the district court was going to deny an evidentiary hearing, nor in their reply brief on appeal, from which we view the lame statement that "space does not permit us to respond to appellees' assertions that the damage claims were not viable" as evidence to the contrary. Appellants rely on *Litton Systems, Inc.* v. *American Telephone & Telegraph Co.*, 700 F.2d 785, 823 (2d Cir. 1983), *cert. denied*, 104 S. Ct. 984 (1984), and other antitrust and damage cases that have adopted the elasticity theory of *Story Parchment Co.* v. *Paterson Parchment Paper Co.*, 282 U.S. 555, 563 (1931); such cases, however, involve damages not to a multimillion member class but to either a single individual plaintiff or a relatively small class of plaintiffs. In sum, and largely because appellants have not argued convincingly to the contrary, we must agree with the district court's treatment of the alleged $200 million loss to the class as a whole, as well as the $39 million loss to policyholders that is drawn from a comparison of the loss ratio implemented by the Associations' current carrier to the loss ratio used by CPG, *see* 588 F. Supp. at 1056-57.[3]

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[3] We find, however, not altogether irrefutable the district court's conclusion that comparing loss ratios could not serve as a method of determining damages in this case. Prudential's willingness to utilize a loss ratio over 14% lower than CPG's average previous loss ratio obviously reflects a commitment prospective in nature, and to that extent is irrelevant to proof of damages here. It is possible, however, that the Prudential loss ratio was not determined whimsically but was projected from data that would form much of the factual basis for the antitrust claims at issue here. A demonstration, however, of the extent to which Prudential's determination of a loss ratio might reveal a method of structuring what to lay persons seems an intimidating mass of data was a task for appellants, not the district court—a task appellants failed to perform. We emphasize the difference between supporting a claim for the relevance of data and supporting a claim on

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We also referred to the possibility of derivative damages, specifically in terms of the "over $19 million" in advertising revenues it is estimated the Associations will obtain from other advertisers "in the next five years alone." 706 F.2d at 435. The district court thought this derivative claim worthless, since N.Y. Not-for-Profit Corp. Law § 623(a) (McKinney 1970) requires that such an action be brought by at least five percent of any class of members. This analysis is incorrect; since the Associations are concededly District of Columbia nonprofit corporations, District of Columbia law controls the maintenance of any derivative action, *see Abramowitz* v. *Posner*, 513 F. Supp. 120, 126 (S.D.N.Y. 1981), *aff'd*, 672 F.2d 1025 (2d Cir. 1982); *see generally* 7A C. Wright & A. Miller, *Federal Practice & Procedure* § 1826, at 328 (1972), and apparently contains no such limitation.

Significantly, however, neither below nor on this appeal have appellants advanced any data that would lead us to think that an assertion of this derivative claim could be litigated successfully; appellants have failed to utilize the opportunity afforded by this court's previous remand to produce "cogent factual objections" to the foreclosure of derivative damages claims on behalf of the Associations. However tantalizing the prospect of a

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the basis of specific data. Because appellants failed to do the former, the district court was well within its discretion to discount the prospect of the latter.

Similarly, we can agree with the district court that a theory of unjust enrichment is inappropriate in proving damages for an antitrust violation, 588 F. Supp. at 1056-57, without rejecting the possibility that, as in *Zeller* v. *Bogue Elec. Mfg. Co.*, 476 F.2d 795, 802 (2d Cir.), *cert. denied*, 414 U.S. 908 (1973), CPG's excess gain might be found the most effective way to measure plaintiffs' loss. But appellants' inability to justify advancing litigation to a stage where that issue would emerge makes the point moot.

derivative claim for lost revenues may be when expressed as a generality, in the absence of data articulating the claim with specificity, the district court's approval of a settlement foreclosing to class members the right to bring a derivative action must be affirmed.[4]

In doing so, we note that the very nature of a derivative claim largely mitigates whatever threat may be posed by the settlement's foreclosure of the right of class members to bring a claim on behalf of the Associations against the defendants because the nearly 3,000 members of the Associations who have opted out of the current lawsuit remain eligible to vindicate injury suffered by the Associations as a result of defendants' alleged illegalities, notwithstanding the district court's approval of the settlement. It is perhaps significant, however, that as yet no one has attempted such a derivative action.

Finally, we called on the district court to examine *Copitka* v. *Colonial Penn Group, Inc.*, No. 442574 (Cal. Super. Ct. San Diego Cty. 1979), a case settled for $500,000 in the heat of the publicity surrounding the soon-to-be-terminated relationship between CPG and the

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[4] In light of Judge Mansfield's vigorous dissenting opinion, we wish to make it clear that we view the viability of class claims for damages solely from the standpoint that they are claims for federal antitrust violations and lost advertising revenues. As such for damage purposes we agree with the district judge that the claims had no viability and rather than be "potentially worth many millions of dollars," as Judge Mansfield suggests, and as our first opinion thought possible, it had no worth. This is not to express any opinion on the value, if any, of the state claims, as we say in the text at 3761. Moreover, it is not as if no monetary recovery were obtained in the settlement; as we pointed out, CPG agreed in the "voluntary" agreement of September 1980 to pay the Associations a total of $6.86 million and to spend an additional $4.5 million to promote membership in the Associations.

Associations. We agree that the case is irrelevant to the issues in this federal antitrust action.

Finding no viable federal antitrust claim for damages is not, of course, to say that there is no state claim for fraud or breach of fiduciary duty of sufficient viability to render unfair and unreasonable a settlement foreclosing such a claim. That determination, of course, is a matter for the state court, which has yet finally to act. The parties' settlement is conditioned upon approval of both the state court and the federal court, so that our judgment affirming approval of the settlement is necessarily subject to the state court's approval but we make it so subject, in any event.

The second factor that we asked the district court to examine is "the negotiating process, examined in the light of the experience of counsel, the vigor with which the case was prosecuted, and the coercion or collusion that may have marred the negotiations themselves." 706 F.2d at 433. The district court's analysis of these issues on remand is somewhat unresponsive. Although, as previously mentioned, the district court attests "to the high professional character of [plaintiffs' attorneys'] work," adding that "[t]here has never been the slightest hint in the conduct of plaintiffs' attorneys that they were willing to sacrifice legitimate claims for an easy settlement," 588 F. Supp. at 1058, we had hoped for more analysis, especially given the temporal relationship between the agreement reached among the defendants in September 1980 and the stipulation of settlement reached among the defendants and plaintiffs two months later. For although in one sense we might agree with the district court that "there was no 'rapid agreement in principle,'" and "[t]he chronology of the litigation makes

this clear," *id.* at 1060, it is precisely the chronology of the litigation that calls into question the vigor and dedication of class representations. For on the basis of chronology alone, it appears, to say the least, that the settlement adds very little to the benefits obtained for the plaintiffs as a result of the voluntary agreement reached in September 1980. Put another way, given only the chronology of this litigation, one might ask, as on the previous appeal we did ask, why the plaintiffs did not simply withdraw their complaints after having obtained, in the agreement of September 1980, substantially all the relief that their litigation in state and federal court sought. On first impression, chronology alone suggests that after the agreement of September 1980, the negotiations leading to the stipulation of settlement amounted to little more than a trade of damages relief foreclosure for attorneys' fees.

Despite the limited assistance from the district court, however, we have been enlightened by the briefs and record on appeal. They indicate an early fruitless round of settlement negotiations in 1979, at which time the Associations began to change the structure of its ties to CPG in a manner directly responsive to allegations made in the state and federal court complaints. Of course, as the objectors suggested in their offer of proof to the district court, no one can be certain whether the decision to separate the Associations from CPG stemmed principally from this lawsuit, or from the pendency of other litigation coupled with investigations by the United States Postal Service and the Securities and Exchange Commission, or from what appellants have termed "a deluge of attendant unfavorable publicity." We do know, however, that this litigation commenced and was proceeding at pace with the development of the record to which we

have alluded above—a significant fact, since it is immaterial as a mater of law whether there were factors involved in the agreement of September 1980 other than the lawsuit. One never can tell the exact motivations of the parties in reaching a voluntary agreement, but it is apparent that we were under a misimpression that the issues addressed in the lawsuit settlement, because resolved subsequent in time to the voluntary agreement, were not a causative factor or a catalyst in bringing about the voluntary agreement. The likelihood that the voluntary agreement might have followed logically, if not chronologically, from litigation directed toward a judicially imposed resolution of the dispute cannot be overlooked, since it is clear that the Associations on the one hand and Leonard Davis and CPG and related companies on the other desired to forestall further unfavorable publicity by "voluntary" agreement.

Of most importance, the district court has made a finding not only that "there was a long and conscientious struggle by the attorneys for both plaintiffs and defendants to achieve an honorable and realistic disposition of this important case," 588 F. Supp. at 1061, but that "[t]he attack mounted by plaintiffs succeeded" as "[f]ew class actions have ever succeeded in altering commercial relationships of such magnitude," *id.* at 1052. On this record, we cannot say that these findings are clearly erroneous, nor do we think it would be prudent judicial administration to remand for further findings in this respect. The experience of counsel and the vigor with which the case was in fact prosecuted indicate that the negotiation process in general was aboveboard, at arm's length, and noncollusive. And once we treat the agreement of September 1980 as caused in substantial part by the suit(s), we cannot ignore the fact that under the "volun-

tary" agreement of September 1980 CPG agreed to pay the Associations a total of $6.86 million and to spend an additional $4.5 million to promote membership in the Associations between January 1, 1980, and June 30, 1981, in addition to its various other agreements relative to disassociation. Eleven million dollars is no small sum.

We come finally to the point that, unfortunately perhaps, constitutes the principal thrust of this appeal, namely, that the attorneys' fees agreed upon in the settlement were negotiated simultaneously with issues on the merits, thereby tainting the settlement. *Cf. Barnett* v. *Pritzker*, 73 F.R.D. 430, 432 (S.D.N.Y. 1977) (viewing class action defendant's presettlement arrangement to pay plaintiff's attorneys' fees in a definite amount as potentially collusive); *City of Philadelphia* v. *Chas. Pfizer & Co.*, 345 F. Supp. 454, 471 (S.D.N.Y. 1972) (expressing concern over simultaneous negotiations for class members and fees). *See generally Developments in the Law—Class Actions*, 89 Harv. L. Rev. 1318, 1608 & n.132 (1976). Appellants argue further that long after agreement on fees had been reached there were settlement drafts and correspondence indicating that negotiations were continuing. And they emphasize that they pressed without success for discovery in this area following remand by this court to the district court. Appellees, in response, assert that fees were discussed only after a "framework of settlement" on the merits had been agreed upon, and that documents in the state court proceeding—now a part of the record in this case on appeal—are sufficient to support this position without additional discovery.

The key to appellants' claims are statements made to the state court referee by Mr. Rosdeitcher, counsel for

CPG, that fees had been discussed during the course of the settlement discussions. Mr. Rosdeitcher, when asked how the number of $2.325 million came about, testified that:

> This was a negotiated figure. During the course of the settlement discussions we were asked whether, among other things, as part of the settlement, we would agree not to oppose a fee of a certain size. And various numbers I can't remember the progression of the numbers, various numbers were discussed.

When asked over what period of time the negotiations took place, Mr. Rosdeitcher responded, "I would say there were two periods . . . of settlement discussion." He then stated that the first discussion of settlement, which included discussion about both the entire settlement and the entire counsel fees, occurred in 1979, when evidently a claim was made for $4 million in attorneys' fees. Under further questioning, Mr. Rosdeitcher testified that in early 1980, CPG would probably not have opposed a sum of $1 million, while the other side was talking about $4 million. He testified before the referee that "through the period in early 1980, we came to an agreement as to the number we would not oppose." Apppellants claim that such testimony proves the occurrence of a simultaneous discussion of merits and fees sufficient to taint the entire settlement.

Appellees' response is that, when read in context, Mr. Rosdeitcher's testimony does not support appellants' claim. Referring to a transcript of the hearing before the referee, appellees point out that during an early round of settlement negotiations in 1979, defendants were asked whether they would agree not to oppose a fee of $4 million. The CPG people responded that they would

not accept any such proposal, whereupon the discussions broke off. In the latter part of 1979 and continuing on into 1980, settlement discussions began anew and a framework of settlement was agreed upon orally. Furthermore, in an affidavit submitted to the state court and now included in our record on appeal, counsel for CPG states that only after the merits of the settlement were accepted in principle did CPG enter into negotiations concerning the maximum fee that it would not oppose, and only at the conclusion of those negotiations did it agree to accept a fee application not in excess of $2.325 million. Affidavits filed in the state court on behalf of the Association and the plaintiffs support the CPG statement—in effect, that only certain minutiae were left for resolution after the matters in principle had been agreed to. The district court, viewing these averments "in light of all the circumstances," said that they appear "entirely credible." 588 F. Supp. at 1061.

We agree. This and other courts have previously expressed concern over the award of attorneys' fees in class action settlements. *See, e.g., Prandini* v. *National Tea Co.*, 557 F.2d 1015, 1020-21 (3d Cir. 1977); *Grinnell I*, 495 F.2d at 468-74. Sharing this concern, we nevertheless find no reason to disturb the district court's determination that the conduct of the parties leading to agreement on attorneys' fees was proper. Here, in contrast to the circumstances in *Prandini*, there is no issue involving allocation of a fund between class damages and attorneys' fees or even a separate award. Instead, the discussion concerned the payment of attorneys' fees alone, presumably in anticipation of the "relief" that plaintiffs would obtain as a result of defendants' agreement of September 1980. Also in contrast to *Prandini*, the course of negotiations on the settlement in general reflects the absence of a

"sweetheart" relationship between negotiating parties, as evidenced by the combativeness of deposition testimony, *see supra* at 3752-53, and by the averment, *supra* at 3766, that the earlier fee negotiations broke off when plaintiffs pressed for a fee considered to be too high. Moreover, as the court in *Prandini* recognized, "with the increasingly heavy burden upon the courts, settlements of disputes must be encouraged." 557 F.2d at 1021. Absent special circumstances, such as those in *Prandini*, the negotiation of attorneys' fees cannot be excluded from this principle. *See White* v. *New Hampshire Department of Employment Security*, 455 U.S. 445, 453 n.15 (1982); *cf. Shlensky* v. *Dorsey*, 574 F.2d 131, 150 (3d Cir. 1978) (refusing to require that approval of damage aspect of settlement precede consideration of attorneys' fees). We do not find such special circumstances here.[5]

Two remaining questions may be dealt with summarily. First, should the Associations, which are indeed made up of the members of the plaintiff class, be re-

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[5] It may be, as Judge Mansfield suggests, that it would be wise not to have the subject of attorneys' fees agreed upon but "be left to the court for determination after its independent review and approval of a settlement . . . ." (dissenting op., at 3775-76). But where, as here, the amount of the fees is important to the party paying them, as well as to the attorney recipient, it seems to the author of this opinion that an agreement "not to oppose" an application for fees up to a point is essential to completion of the settlement, because the defendants want to know their total maximum exposure and the plaintiffs do not want to be sandbagged. It is difficult to see how this could be left entirely to the court for determination after the settlement.

I note with interest Judge Newman's doubts about a defendant's "clear sailing" clause and the distinction that he draws between such a clause and a plaintiff's "ceiling" clause. In my view, as a practical matter, I believe it a distinction without a difference.

quired to pay any part of the settlement?[6] 706 F.2d at 436. Second, why was a bonus awarded "regardless of the difficulty of the tasks performed"?[7] *Id.* at 435. The district court answered the first question affirmatively, stating that, it being "settled law that attorneys' fees may be charged against the beneficiary of a class action . . . [the Associations'] agreement to a modest contribution toward the attorneys' fees was entirely reasonable and lawful." 588 F. Supp. at 1061.

On further consideration, we agree. The similarity between this case and *Shlensky*, 574 F.2d at 150, is instructive. In *Shlensky*, plaintiffs' derivative action on behalf of the Gulf Oil Corporation sought, inter alia, recovery of corporate funds illegally expended in certain election campaigns. The parties agreed to a stipulated settlement that included an agreement by Gulf to reimburse plaintiffs' attorneys and accountants for up to $600,000 in fees and $25,000 in expenses. On appeal from the district court's approval of the settlement, the Third Circuit rejected the objector's claim that Gulf's agreement

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[6] According to the terms of the settlement, the defendants are not to oppose plaintiffs' application for attorneys' fees and expenses not in excess of $2.325 million. Of those fees and expenses not in excess of $1 million, CPG is to pay 90% and the Associations the remaining 10%. Of any fees and expenses in excess of $1 million, CPG is to pay 70% and the Associations the remaining 30%. The plaintiffs did in fact apply to the state court referee, as well as to the district court, for the full $2.325 million, and both the referee and the district court approved the application, the district court approving the application again on remand, 588 F. Supp. at 1061.

[7] In the previous appeal, we incorrectly described the magnitude of the bonus approved by the referee and the district court as applying a multiplier of two to the average hourly rate of $120. The district court informs us, 588 F. Supp. at 1059, that a multiplier of 1.685 more accurately reflects the bonus over the average hourly rate, given the 10,282.75 hours submitted by plaintiffs' co-counsel to justify an application for $2,085,901 in fees.

to pay plaintiffs' fees and expenses contributed to a settlement that was unfair and unreasonable because Gulf would be left without a net benefit. In so doing, the court found nothing improper in Gulf's agreement to pay fees and expenses totaling $625,000, where as a result of the settlement Gulf's monetary benefit alone would total $2,875,000.

Here, as in *Shlensky*, a party purportedly harmed by defendants' allegedly illegal conduct agreed to pay a part of plaintiffs' attorneys' fees. In *Shlensky*, the court found reasonable Gulf's assumption of $650,000 in plaintiffs' fees and expenses in light of Gulf's net gain of $2,875,000 from the settlement. *Id.* Here, where the Associations' contribution of several hundred thousand dollars to plaintiffs' fees and expenses is part of a settlement whereby CPG will pay to or spend on behalf of the Associations a total of over $11 million, *see supra* at 3763-64, the contribution is a fortiori reasonable.

Moreover, the settlement brings to the Associations substantial nonmonetary benefits; it is quite evident from the affidavit filed by Cyril F. Brickfield, the Executive Director of the Associations and a party defendant to this action, that the Associations were desirous of ending the litigation as well as terminating the relationship with CPG, because it was interfering with the conduct of business of the Associations, was a cloud on their reputations and was discouraging voluntary service leaders as well as professional staff. The Brickfield affidavit points out that without the Associations' participation in the fee provision an agreement would not have been reached; and had the agreement failed, the Associations would have been faced with legal fees in further defense of the suit, as well as the other costs inherent in litigation. We think

that these considerations justify the payment of fees by the Associations, but not with the bonus multiplier that was applied by the district court; we therefore reduce the attorneys' fees payable by the Association to $252,683.[8]

For the reasons stated in the district court opinion, 588 F. Supp. at 1059-60, we agree that the award of attorneys' fees and costs may otherwise stand.

Settlement as modified approved, subject to approval of the state Supreme Court in *Conway* v. *Davis*. No costs to any party.

JON O. NEWMAN, *Circuit Judge*, concurring:

In concur in Judge Oakes' comprehensive opinion and write these additional words only to express a caution concerning the continued use in settlements of a "clear sailing" clause whereby a defendant agrees not to challenge a plaintiff's request for attorney's fees up to a stipulated amount.

It has long been recognized that any agreement concerning plaintiff's attorney's fees, entered into in the course of settling litigation, poses a danger of pitting the interests of the plaintiff in receiving a recovery against

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[8] We arrive at this figure by calculating, according to the agreed upon contribution formula, *supra* note 4, the Associations' share of plaintiffs' requested fee of $2,085,901 to be $425,700, and then reducing it by a divisor of 1.685. Because CPG's contribution is, of course, unaffected by the elimination of the multiplier as applied to the Associations' contribution, the effect of the foregoing modification is a reduction of plaintiffs' fee award from $2,085,901 to $1,912,814. The net result is that CPG's contribution to plaintiffs' fees remains at $1,660,131, while the Associations' contribution is reduced to $252,683.

the interests of the plaintiff's attorney in receiving a fee. The tension between their interests exists even in the garden-variety tort cases in which the attorney has an agreement to receive a contingency fee at a stated fraction of the recovery. The attorney, anxious to assure himself a fee, may urge a settlement at a low figure, contrary to the position of the plaintiff, who might be willing to take the risk of no recovery for the chance to win a larger recovery. Or the plaintiff may be anxious to assure himself a recovery and therefore favor settlement at a low figure, contrary to the position of his attorney, who might be willing to take the risk of receiving no fee for the chance to win a larger fee based on a larger recovery.

These potential conflicts between a plaintiff and his attorney arise in the context of cases proposed to be settled for a cash payment from the defendant, out of which the plaintiff's attorney receives a fee. In that context, the defendant is indifferent to the amount of the fee that results from an allocation of the payment between the plaintiff and the plaintiff's attorney. The defendant's interest is in knowing his total exposure.

However, the defendant's interest in ascertaining the amount of the fee of the plaintiff's attorney vitally affects the settlement of cases like the present one in which the settlement does not provide a fund but calls only for injunctive relief, and the plaintiff's attorney is entitled to a fee for having conferred a benefit upon the members of the class.[1] In this circumstance, the defendant is entitled

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[1] The defendant would also want to ascertain the amount of the plaintiff's attorney's fee in the settlement of any case in which the plaintiff, whether or not representing a class, is entitled to recover an attorney's fee by virtue of a statute authorizing an attorney's fee to the prevailing party. *See, e.g.*, 42 U.S.C. § 1988 (1982).

to know the limit of his total exposure, and, as the Supreme Court has recognized, it is unrealistic to expect him to agree to a settlement concerning the injunction terms until he knows the limit of his exposure for the attorney's fees. *See White* v. *New Hampshire Dep't of Employment Security*, 455 U.S. 445, 453-54 n.15 (1982); *see also* A. Miller, *Attorneys' Fees in Class Actions, A Report to the Federal Judicial Center*, 219 (1980). The settlement terms that benefit the plaintiff class all have a cost to the defendant, and the defendant will be more likely to settle when a limit upon all his costs has been determined. Thus, settlements are promoted by permitting the parties to a class action to negotiate a ceiling on the amount of attorney's fees that the plaintiffs will seek.

However, a *plaintiff's* agreement not to seek attorney's fees above a stipulated ceiling must be distinguished from a *defendant's* agreement not to contest an application for fees up to the amount of that ceiling. The two agreements differ in fundamental respects. The negotiated ceiling restricts the plaintiff; the "clear sailing" clause restricts the defendant. When only a "ceiling" clause is used, though the plaintiff will almost always make a claim equal to the amount of the ceiling, the figure awarded by the court will not necessarily be so high and may frequently be considerably less; the defendant has a strong incentive to persuade the court to award some figure below the ceiling, since it will save from its anticipated maximum exposure any dollar below the ceiling that is not awarded in fees. But when a "clear sailing" clause is used and the fee application is not challenged by the defendant, the figure allowed by a trial court will tend to be very close to, and frequently precisely at, the negotiated ceiling, as occurred in this case.

A "clear sailing" clause has two adverse effects that cast substantial doubt on the legitimacy of its use. First, it deprives the trial court and a reviewing court of the certainty of having the propriety of the fee request tested in the adversary process. Sometimes, as in this case, objectors will come forward to challenge the reasonableness of the attorney's fee claimed by the plaintiffs, even when the fee is within the negotiated ceiling. But a "clear sailing" clause creates the risk that a fee request within the negotiated ceiling will not be challenged, placing upon the courts the burden of examining the basis for the fee, unaided by the challenges of an adversary party. *See Prandini* v. *National Tea Co.*, 557 F.2d 1015, 1020-21 (3d Cir. 1977); *Foster* v. *Boise-Cascade, Inc.*, 420 F. Supp. 674, 678, 689 n.8 (S.D. Tex. 1976) (agreed upon fee), *aff'd*, 577 F.2d 335 (5th Cir. 1978) (per curiam). Second, the clause creates the likelihood that plaintiffs' counsel, in obtaining the defendant's agreement not to challenge a fee request within a stated ceiling, will bargain away something of value to the plaintiff class. It is unlikely that a defendant will gratuitously accede to the plaintiffs' request for a "clear sailing" clause without obtaining something in return. That something will normally be at the expense of the plaintiff class. *See* A. Miller, *supra*, at 219-20.

An agreement whereby the plaintiffs agree to place a limit on the amount of attorney's fees to be sought does not encounter similar objections. The amount of the fee ultimately allowed always remains subject to the adversary process. Moreover, the agreement not to seek fees above a stated sum represents a concession on the part of the plaintiffs and their counsel, rather than a

benefit for which the defendant may expect something in return.[2]

In future cases it may be well to scrutinize carefully the use of "clear sailing" clauses. Perhaps they should be forbidden in all cases. Since the parties in this case had no reason to doubt the propriety of agreeing to the clause, I do not object to its use in this case.

MANSFIELD, *Circuit Judge* (Dissenting):

I respectfully dissent. In my view the proposed settlement is tainted by the simultaneously-negotiated agreement by the defendants not to oppose their paying $2,325,000 to class counsel. This amounts to an average of at least $203 per hour for every lawyer, no matter how junior, who worked on the case, plus costs and disbursements. I find it difficult to believe that this huge sum could not have improperly tempted class counsel to give up class claims potentially worth many millions of dollars rather than carry on the fight to enforce those claims or negotiate a more advantageous settlement for the class

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[2] At least this is so whenever the plaintiffs propose a fee ceiling that they will not exceed, and the defendant gladly agrees to incorporate this assurance into the proposed settlement. The risk that a defendant will extract a concession from the class is also normally absent when the defendant holds out for a fee ceiling lower than that initially proposed by the plaintiffs. Perhaps, in some instances of the latter type, a defendant, bargaining about the fee ceiling, might suggest its willingness to accept a ceiling closer to the plaintiffs' demand if the plaintiffs will surrender some benefit unrelated to the fee. The occasional occurrence of this sort of bargaining about the amount of the ceiling is far less troublesome than the negotiation of a "clear sailing" clause, which always confers a benefit upon the plaintiffs and their counsel for which the defendant will always be tempted to demand something in return.

members. Certainly class counsel should bear the heavy burden of proving that they were not so improperly influenced. I do not believe that this burden has thus far been sustained. As the guardian of 11.2 million absent class members unable to protect their own interests, *see National Super Spuds, Inc.* v. *New York Mercantile Exchange*, 660 F.2d 9, 20 (2d Cir. 1981), we should not approve the settlement or the fees until they have done so.

What may be good for class counsel may not necessarily be in the best interests of the class. Although an agreement by defendants "not to oppose" a $2,325,000 fee to plaintiffs' counsel does not technically bind the court, it is naive not to recognize that as a practical matter it constitutes a joint invitation by the parties to the court to award the specified upper limit since the defendants, not the members of the class, would pay the agreed-upon fee and the payment would be in addition to the defendants' commitments under the main settlement. The defendants' interest in learning of their total potential exposure could be satisfied by their obtaining from the class counsel, before joining in a submission of the proposed agreement on the merits to the court for approval, a statement of the fee that the class would seek to have approved and fixed by the court. If that proposed fee figure appeared to the defendants to be excessive they would remain free to withdraw completely from the settlement or to oppose the class counsel's fee application. Advance fee agreements, however, such as the one presently before us, should be abolished since they promote a potential abuse of trust and conflict of interest on the part of class counsel.

For these reasons the amount of the fee should in my view be left to the court for determination after its independent review and approval of a settlement, governed by

the factors outlined in *Hensley* v. *Eckerhart*, 461 U.S. 424 (1983); *Blum* v. *Stenson*, —— U.S. ——, 104 S. Ct. 1541 (1984); *City of Detroit* v. *Grinnell Corp.*, 495 F.2d 448 (2d Cir. 1974); *Lindy Bros.* v. *American Radiator*, 487 F.2d 161 (3d Cir. 1973). Included among the factors to be considered, of course, are the degree of risk incurred by class counsel and whether it justifies a risk premium.[1] The objective should be to compensate class counsel adequately and at the same time not unreasonably reduce the recovery and relief to be gained for the class. However, as Judge Oakes recognized in asking the district court in his earlier opinion, *Malchman* v. *Davis*, 706 F.2d 426, 436 (2d Cir. 1983), to explain whether "the fees [were] agreed upon before the settlement was reached or only after substantive issues were worked out," simultaneous negotiation of attorney's fees and settlement terms poses the serious danger of collusion, *i.e.*, that plaintiffs' counsel will give up potentially valuable client's rights in return for non-opposition to fees higher than those that might otherwise be awarded. *See Barnett* v. *Pritzker*, 73 F.R.D. 430 (S.D.N.Y. 1977); *City of Philadelphia* v. *Chas. Pfizer & Co.*, 345 F. Supp. 454, 471 (S.D.N.Y. 1972). That danger is great in the present case for the reason that we are dealing with the release of claims for very large amounts of money.

The district court, after characterizing as "realistic" and unchallenged an estimate that "individual damage

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[1] In the present case, for instance, the court would also take into consideration the defendants' adoption in February 1979 of some salutory provisions beneficial to the class, which possibly had the effect of assuring class counsel that they were likely in any event to receive some award from the court. As the district court noted, "the vigorous prosecution of these lawsuits was the principal cause, if not the sole cause, of the revisions in practice carried out by the Associations commencing in February 1979."

recoveries would likely be less than $100" (which could result in a recovery of up to $250,000,000) estimated that if the plaintiffs could prove that they would have been able to purchase insurance from another company at 10% less than the premiums charged by Colonial Penn Group (CPG), the savings, after trebling, would be $32.40 per year per person for the 2.5 million members of the class who purchased insurance. This would amount to a potential recovery of $80,000,000 per year. Even if, allowing for the risks and difficulties in proof described by the court, the recovery were cut by 50% it would be $40,000,000 per year for a period of up to seven years. To prepare and try damage claims to completion would be costly and involve substantial risk for plaintiffs' counsel. On the other hand, the settlement, under which the defendants agreed not to oppose $2,325,000 for class counsel's legal fees, assures the latter a virtually riskless award of a very substantial amount for their services. This tantalizing prospect can tempt class counsel, consciously or not, to agree to settlement terms that are less favorable to their clients than would otherwise be the case.

The majority and Judge Griesa, relying on conclusory statements made in counsels' affidavits, have proceeded on the erroneous assumption that class counsel's attorney's fees were not negotiated until after the substantive terms of the main settlement were agreed upon and that the settlement was therefore not tainted by the agreement on class counsel's attorney's fees. The record before the state court Referee (which Judge Griesa apparently did not examine) strongly supports an inference that only after plaintiffs' counsel were assured of non-opposition by the defendants to their $2,325,000 fee application (originally class counsel demanded $4,500,000)

did they surrender their clients' potential recovery of $40 to $80 million per year.

In a hearing on January 9, 1981, only two months after the settlement was reduced to writing and signed by the parties, Mr. Rosdeitcher, CPG's counsel, was asked by Referee Johnson, "[h]ow did the number of $2.325 million [maximum legal fees] come about?" Rosdeitcher replied that it was a "negotiated figure" arrived at during the "settlement discussions . . . as part of the settlement." [2] He stated that in February 1979 (when settlement of the case was initiated and long before terms were agreed upon) counsel for the parties, including himself, discussed "both the form of a settlement" and "whether we [defendants] would be agreeable not to oppose a certain fee application." (Suppl. App. 4).[3] At this

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[2] "THE REFEREE: Mr. Rosditcher, how did this number come about, is what I would like to know? How did the number of 2.325 million come about? Where did that come from?

"MR. ROSDITCHER: This was a negotiated figure. *During the course of the settlement discussions, we were asked whether, among other things, as part of the settlement, we would agree not to oppose a fee of a certain size. And various numbers, I can't remember the progression of the numbers, but various numbers were discussed.*

"THE REFEREE: Who discussed them, if I may ask?

"MR. ROSDITCHER: I discussed them with Mr. Lesch. Mr. Kalmus discussed them with Mr. Lesch. Mr. Malchman and Mr. Kaufman, I believe, were also involved in discussions. Mr. Belnick was involved in discussions. And a partner of mine, Arthur Kalish, and at one point, one of my senior partners, Morris Abram, had been in one early discussion." (Suppl. App. 2-3). (Emphasis supplied).

[3] "THE REFEREE: How long did these negotiations or discussions ensue? Over what period of time?

"MR. ROSDITCHER: I would say there were two periods, and correct me if my memory is inaccurate, there were two periods of settlement discussion.

There was a period which went back, I suppose, to, was it late 1978?

"MR. BELNICK: Yes.

[Footnote continued on following page]

early stage plaintiffs' counsel, Mr. Lesch, asked the defendants whether they would agree not to oppose an application by the plaintiffs for an attorney's fee of ap-

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"MR. LESCH: *In about February, 1979.*

"MR. KALMUS: Which came to nothing.

"MR. ROSDITCHER: *Which was the first discussion of settlement. It was at that time—*

"THE REFEREE: *Settlement with reference to the counsel fees, I'm talking about specifically now.*

"MR. ROSDITCHER: *Both, the entire settlement and entire counsel fees.*

The Associations at that time had begun the process of effecting changes in the relationship and the structure of the Association, and so forth, that Mr. Lesch has been describing and described in his affidavit, at that time.

And it was about that time that settlement discussions were first raised with any seriousness.

My recollection is that at times, people have said, 'Is there any basis for settlement?' But it was nothing worth describing here.

And at that time [early 1979] we discussed both the form of a settlement and the question of fee was raised, as to whether we would be agreeable not to oppose a certain fee application.

Now, I don't recall what amount was proposed. I believe that it was certainly in excess of the 2.3 million.

"MR. LESCH: So the record is clear,—

"THE REFEREE: Let Mr. Rosditcher state it, and then you may have the opportunity.

"MR. LESCH: Excuse me.

"THE REFEREE: After Mr. Rosditcher, Mr. Kalmus will state it, and you will state it and anyone else.

Go ahead.

"MR. ROSDITCHER: My recollection is there was an initial figure which was substantially in excess of 2.325 million dollars mentioned.

"THE REFEREE: Which was it, approximately?

"MR. ROSDITCHER: Which was approximately $4 million.

"THE REFEREE: When you say mentioned, mentioned by whom?

"MR. ROSDITCHER: Mentioned by plaintiffs' counsel.

"MR. LESCH: *So the record is clear, you are talking about 1980?*

"MR. ROSDITCHER: *No, talking about 1979.*" (Suppl. App. 3-5). (Emphasis supplied).

proximately $4.5 million,[4] but the CPG and Association defendants were unwilling to agree to such a large amount. Settlement negotiations were then suspended, according to Messrs. Kalmus and Rosdeitcher, who proposed "in early 1980" that the fee be limited to $1 million.[5] Out of these negotiations, which began in 1979

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[4] "MR. LESCH: . . . .

First, on the question of fee negotiations, I do not believe that Mr. Fischman ever mentioned the figure of $4 million.

What I believe happened was that benefits were discussed. And that in the context of the quantification of benefits, the inference was drawn that Mr. Fischman was talking about a fee of $4 million.

My understanding is that the first time that that figure was mentioned occurred in negotiations between, and I don't believe it was 4 million, I believe that the number I mentioned was somewhat in excess of 4 million.

"MR. KALMUS: I believe it was. 4½.

"MR. ROSDITCHER: I think Mr. Lesch is correct in the way I first got the 4 million.

"MR. KALMUS: I would concur with Mr. Lesch.

"MR. ROSDITCHER: I derived the inference from the benefits they were describing.

"MR. LESCH: *And that then we got into the negotiations and we started with the figure in excess of 4 million, and they started with a figure substantially below 2.325 million dollars.*" (Rev. Suppl. App. 17-18). (Emphasis supplied).

[5] "MR. ROSDITCHER: And we indicated, that is, the CPG and the Association defendants as well, we would not be agreeable to an agreement which said we would not oppose such a fee.

"THE REFEREE: Such a fee of $4 million?

"MR. ROSDITCHER: Yes.

"THE REFEREE: Very well. But did you come back with a counter-proposal with reference to the—

"MR. ROSDITCHER: Not at that time, I think our feeling was it was too high, and didn't come back with any approval.

I think at some point, shortly after those talks began, that is, within a month or two, they ended, and we then proceeded to full activity.

I think things got wound up and we went through a lot of discovery after that.

The next period that I recall, the time is collapsing here.

[Footnote continued on following page]

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"THE REFEREE: I realize that.

"MR. ROSDITCHER: Was it early in 1980 we began again?

"MR. KALMUS: In the latter part of 1979.

"MR. ROSDITCHER: The latter part of 1979, yes.

"MR. KALMUS: I first had some discussions then. I and Mr. Oberman, my partner, had discussions with Mr. Lesch and his partner, Mr. Fischman. And at times, with Mr. Malchman and Mr. Kaufman as well.

"THE REFEREE: With reference to counsel's fees?

"MR. KALMUS: No, not specifically; with reference to the possibility of settling the litigation either with the AARP defendants alone or the entire litigation as to everyone.

Those discussions began in late 1979, continued into 1980, on and off, with adversary discovery going on concurrently.

In due course, in the early spring, I would say, of 1980, or perhaps late winter of 1980, that is to say, a little less than a year ago, those discussions led to discussions in which Colonial Penn counsel, Mr. Rosditcher and his partner, Mr. Kalish, were also involved, *that went on back and forth over an extended period of time into June of 1980.*

At that time, a framework of a settlement was agreed upon orally. That framework included an understanding that the defendants would not oppose an application for counsel fees up to $2.325 million, inclusive of disbursements.

And from June through into the autumn of last year [1980], we worked on the details of a settlement agreement which resulted in the settlement agreement that you have before you dated November 3, 1980.

"THE REFEREE: Is that substantially what occurred, Mr. Rosditcher?

"MR. ROSDITCHER: That is substantially what occurred.

Just to add to something that I said earlier, I do not recall that you asked how we got to this number.

"THE REFEREE: Yes.

"MR. ROSDITCHER: And I do recall that Mr. Lesch, I believe it was, told us precisely what he believed the total hours spent by his firm and the Kaufman firm were worth. *And I believe the number mentioned at that time, this was probably in early 1980, was a million dollars.*

He also felt that the benefits he conferred justified a substantial multiple of that number.

And I think that we then started—said 4 million, and we said, 'No, that is too high.'

And somehow, *through the period in early 1980, we came to an agreement as to the number we would not oppose.*" (Suppl. App. 6-9). (Emphasis supplied).

with class counsel initially asking $4,500,000 and defendants starting with $1,000,000, came the figure of $2,325,000 which, according to defense counsel, constituted part of a "framework of settlement" agreed to orally in June of 1980.

Defendants now contend that their early discussions, in which class counsel asked for a $4,500,000 fee and the defense responded with an offer not to oppose a $1,000,000 fee, should not be considered by us since the parties failed to reach a settlement agreement with respect to the class' claims and discussions then ended, not to be resumed until some time in 1980. If, as defense counsel now concede, it would be improper to discuss class counsel's legal fees until the framework of a settlement of the class claims had been agreed upon and if, as they now aver, there was no discussion of the $2,325,000 legal fee until such an agreement was reached in the latter part of 1980, how do they justify the *earlier* fee discussions which admittedly took place *before* any settlement with respect to the substantive issues was reached? The answer is that the parties *were* discussing the amount of class counsel's legal fee (i.e., $4,500,000 versus $1,000,000 maximum) *before* any agreement on the class' claims was arrived at and, to use Mr. Rosdeitcher's words, the $2,325,000 figure "was a negotiated figure," arrived at "[d]uring the course of the settlement discussions . . . as part of the settlement." See *footnote 2, supra.*

Thus, according to the January 9, 1981, record before Referee Johnson, which was much closer to the events in question than today, the parties acknowledged that they had agreed, long before the terms of the settlement had firmly been reached, that the $4.5 million attorney's fee limit originally sought by plaintiffs' counsel would be

reduced to $2,325,000 and that this figure would not be opposed by the defendants. Against this background it is beyond dispute that the parties did not agree upon the terms of the settlement itself (as distinguished from the amount of counsel fees) until September 1980 and that no written agreement was signed until November 3, 1980. Until the latter date plaintiffs were as a practical matter not legally bound to surrender their damage claims potentially worth many millions of dollars.

From the foregoing record of the hearing before Referee Johnson, in which lead counsel for all major parties participated, it is difficult not to conclude that plaintiffs' counsel were unwilling to give the class' damage claims of some $40-$80 million per year until they were firmly assured that there would be no opposition to their proposed $2,325,000 in legal fees. But, regardless whether one accepts this inference, the record certainly dictates a more searching inquiry than that made by Judge Griesa.

In my view such an inquiry is mandated by other surrounding circumstances as well. The lead plaintiff, Nathan Malchman (whose deposition was never taken), is the brother of Irving Malchman, legal counsel for the class. One of the original named plaintiffs, Frieda Lederer, was Irving Malchman's mother-in-law. Greta Conway is the sister of the chauffeur for class counsel. Louis Stone is a personal friend of class counsel. All of this raises the question of whether, absent these close relationships, the named plaintiffs would not, because of their desire to see their relative or friend receive a generous share of the $2,325,000 legal fee, be much more willing to give up their potential recoveries than would

the other eleven million plus members of the class who have no such relationships with class counsel.

For these reasons I would remand the case to the district court for a more searching inquiry into the reasonableness of the settlement. I would also make clear that the agreement of the defendants to pay class counsel fees up to $2,325,000 should not influence the court in any way not to disallow that amount and fix a substantially lower figure if such a figure appears to be reasonable. Indeed, the district court might test the reasonableness of the attorney's fees agreement by obtaining the benefit of the views of an independent expert or of an adversarial presentation as to the fairness of the $2,325,000 figure.

APPENDIX B

APPENDIX B

MALCHMAN (Nathan), Frieda Lederer and Gerta C. Conway

v.

DAVIS (Leonard), Sophie Davis, Colonial Penn Group, Inc., Colonial Penn Franklin Insurance Company, Intramerica Life Insurance Company, National Association Plans, Inc., American Association of Retired Persons, Carrie B. Allen, Oranda Bangsberg, Bernard Berggren, June Biggar, Arthur Bouton, Mamie R. Capellen, Verna A. Carley, French E. Dennison, Fred Faassen, Jerry P. Johnson, Olaf Kaasa, Clara L. Kleweno, George W. Schluderberg, Floyd E. Tumbleson, Kenneth J. Waite, Alice Van Landingham, J. Leonard Johnson, Melvin Thompson, C.E. Carmichael, Francis C. Seely, Harriet Miller, American Association of Retired Persons Insurance Trust, Dorothy M. Crippen, Edward J. Wenig, James J. Browning, Arthur Schuettner, Lloyd I. Singer, Cyril F. Brickfield and John J. MacWilliams.

No. 77 Civ. 5151.

United States District Court
S.D. New York.

June 8, 1984.

* * *

GRIESA, District Judge.

On May 2, 1983 the Second Circuit reversed and remanded this court's approval of the settlement in this action and approval of counsel fees. *Malchman v. Davis,* 706 F.2d 426 (2d Cir.1983).

Upon reconsideration in light of the remand, the court determines that the settlement is fair and reasonable and that plaintiffs' counsel are entitled to attorneys' fees and disbursements of $2.325 million.

FACTS

The background facts are well summarized in the Court of Appeals opinion as follows:

> This litigation and the companion state court action, *Conway v. Davis,* No. 10535/76 (N.Y.Sup.Ct., N.Y.Cty.), principally arise from the relationship between Leonard Davis and various corporate entities owned or controlled by him and two nonprofit organizations of elderly persons, the National Retired Teachers Association (NRTA) and the American Association of Retired Persons (AARP).
>
> Dr. Ethel Percy Andrus, a retired California high school principal, founded the NRTA in 1947 to promote the interests of retired teachers. In 1956, at Dr. Andrus's request, insurance broker Leonard Davis persuaded a national insurance company to underwrite a voluntary group health insurance program for the members of NRTA. In 1958, again with Davis's help, Dr. Andrus formed the AARP to serve the interests of Americans over 55 years old. AARP offered voluntary group health insurance to its members similar to NRTA's. Since their founding, the two associations have attracted millions of members and presently have, between them, over 13 million members throughout the United States. Meanwhile, Davis formed the companies that in time became Colonial Penn Group (CPG) to underwrite health insurance policies in group plans and to provide other services to the associa-

> tions' members. From 1958 on Davis and his companies managed the AARP and NRTA insurance plans. The associations encouraged their members to purchase insurance, travel and other products and services exclusively through Davis-controlled entities, including insurance subsidiaries, group travel companies, and employment agencies. Davis's entities, moreover, had the exclusive right to advertise in the associations' publications and were permitted to do so at what appears to be substantially less than the fair market value of such advertising. CPG also maintained the membership lists of the associations in its computers.
>
> As AARP and NRTA grew, so did Colonial Penn and its various subsidiaries, its total revenues being $171 million in 1972 and $445 million in 1976. The AARP/NRTA health insurance plans generated over $261 million in premiums in 1977. As of January 1, 1976, CPG led 929 major United States corporations in profitability with a five-year average annual return on capital of 33.5% a figure nearly double the profitability of either IBM or Xerox and three times greater than the median return of 11.3% for the entire insurance industry.

706 F.2d at 427-28.

This litigation was commenced initially in Supreme Court, New York County on May 4, 1976. The complaint was filed on behalf of Frieda Lederer as representative of the class of AARP members who had purchased group health insurance from CPG on AARP's recommendation. At a subsequent time, Frieda Lederer died and other named plaintiffs were added. The suit was against CPG, Davis and other defendants. The complaint sought injunctive relief only and no damages. The original counsel for

plaintiffs was the law firm then known as Kaufman, Taylor, Kimmel & Miller (presently Kaufman Malchman & Kirby). Defendants promptly moved to dismiss the complaint. While the motion was pending, the firm then known as Shea, Gould, Clemenko & Casey (now Shea & Gould) appeared as co-counsel for plaintiff. The original complaint was dismissed upon consent with leave to replead. An amended complaint was filed in the state court action in July 1977. Gerta Conway was named as an additional plaintiff, and the state court action thereafter carried the name *Conway v. Davis.* The amended complaint alleged that defendants had committed fraud and breach of fiduciary duty in arranging with CPG for group health insurance and other services to be offered to AARP members. The amended complaint alleged that AARP had entered into improper arrangements with CPG, and had failed to select independently a group health insurance carrier and purveyors of other services which would be recommended by AARP.

In October 1977 Lederer and Conway, joined by Nathan Malchman, commenced the federal court action. It was brought as a class action under the federal antitrust laws. The class, as described in the complaint, consisted of the insurance-buying members of AARP. The federal action was basically the same as the state action, except that the federal action was based on the antitrust theory.

Between November 1977 and May 1978 there was motion practice in the state court action. Defendants' attempt to dismiss the action was unsuccessful, and defendants served their answers in the state court action in June 1978.

Discovery commenced in the state action on June 12, 1978 when defendants served interrogatories and document requests. In July 1978 plaintiffs served document re-

quests. In response to the mutual document requests, plaintiffs, produced over 4,000 pages of documents and defendants produced over 100,000 pages of documents, of which plaintiffs made copies of over 65,000 pages.[1] Plaintiffs also filed lengthy answers to interrogatories.

The parties chose, for good and sufficient reason, to conduct almost all their discovery in the state court action. It is easy to understand why this was so. The litigation originated in the state court. Moreover, motion practice directed to the sufficiency of the complaint was completed early in the proceedings. There was no question of the jurisdiction of the state court over the fraud and breach of fiduciary duty claims, as there was in the federal court action, where subject-matter jurisdiction was seriously challenged, as will be described later in this opinion. In any event, it was understood that the state court discovery would be used in the federal court action.[2]

Depositions in the state court action commenced in January 1979. Plaintiffs deposed fourteen persons. Defendants deposed four persons. These depositions were conducted through mid-May 1980. There were sixty-six days of testimony resulting in 11,850 pages of transcript. There were numerous disputes during the discovery resulting in applications to the state court.

Plaintiffs moved in the state court action on January 8, 1979 for an order certifying the class. Defendants objected

[1]The Court of Appeals, after referring to defendants' request for documents, states, "As of early 1979, plaintiffs had obtained little or no discovery information from defendants." 706 F.2d at 429. The Court of Appeals omits reference to the 100,000 pages of documents obtained by plaintiffs from defendants thereafter.

[2] The Court of Appeals states, "No discovery at all was undertaken by plaintiffs in this [the federal] action." 706 F.2d at 429. As noted in the text, the state court discovery was intended to apply in both actions.

on the ground that they had not completed discovery on the adequacy of the representatives. On February 15, 1979 it was stipulated in the state court action to withdraw the motion for class certification until further discovery had been completed.

To return to the federal action, on August 11, 1978 a motion was filed to dismiss the federal complaint on the grounds that the action was barred by § 2(b) of the McCarran-Ferguson Act, 15 U.S.C. § 1012(b), and that plaintiffs lacked standing to assert the antitrust claims. Extensive briefs were filed on this motion. The questions presented were of considerable difficulty. The court requested further submissions and stipulations of fact. This additional work was completed in April 1980.

By the spring of 1980 serious settlement negotiations were taking place. One immediate result of this was that on June 16, 1980 the parties requested the federal court to withhold decision of plaintiffs' motion to dismiss.

The following events relating to the ultimate settlement of the action occurred. In February 1979 AARP and NRTA both passed a series of resolutions which provided for the discontinuance of their endorsement of certain CPG products *other than* group health insurance, and authorized a study of health insurance programs to determine whether the Associations' arrangement for group health insurance with CPG should continue after the then current term expired in June 1981.

In January 1980 the Associations decided to initiate a competitive bidding process to determine who would underwrite the group health insurance programs after June 1981. On September 1, 1980 the Associations signed an agreement with CPG. At least one of the purposes of

this agreement was to provide for the transition from CPG to another insurer in the event that CPG was not selected for the health insurance programs commencing in July 1981. The agreement provided in detail for transitional arrangements in the event a new carrier was chosen and provided for uninterrupted coverage for insured Association members. It also provided that CPG would transfer the custody and maintenance of the Associations' membership lists to the Associations.

Another feature of the September 1, 1980 agreement was that CPG would pay the Associations a total of $6,866,664 and would spend not less than $4.5 million to promote membership in the Associations for the period through June 30, 1981.

A Stipulation of Settlement regarding the state and federal actions was entered into on November 3, 1980. This is the settlement agreement which is before the court. The stipulation provided that:

> 1. The Associations would not enter into a contract with any insurance carrier to underwrite their group health insurance programs for the period from July 1, 1981 except through the request for proposals procedure initiated in early 1980.
>
> 2. The selection of any group health insurance carrier would be made by the boards of directors of the Associations in consultation with the trustees of the AARP and NRTA insurance plans. The boards of directors would consider, among other factors, premium levels, claim service and marketing abilities which would be most advantageous for the members of the Association.

3. The trustees of the insurance plans would serve for periods not exceeding six years and would be solely responsible to the boards of directors of the Associations.

4. The Associations would accept advertising for their magazines and news bulletins from any party at the prevailing rate schedule, subject to limitations which the boards of directors of the Associations might impose with regard to the appropriateness of the subject matter. Such limitations could not restrict advertising to the products and services of one advertiser.

5. Not later than July 1, 1981 the Associations would obtain new data processing and new membership promotion services, previously provided by CPG.

6. Honorary Presidents (one of whom is Leonard Davis) would attend board of directors and executive committee meetings only upon specific invitation, and would not attend any meeting at which the endorsement of any product or service by the Associations was to be considered.

7. No officer or director of CPG, other than the current Honorary Presidents, would be permitted to attend any board of directors or executive committee meeting except upon special invitation and for the limited purpose of presenting information.

8. No officer or director of CPG, other than the current Honorary Presidents, would hold any position in the Association.

9. In the event that the boards of directors of the Associations determined to endorse or

> recommend products or services in addition to group health insurance, the Associations would not limit their endorsements solely to the products and services of one vendor.

These provisions to some extent confirmed the resolutions of February 1979 and other steps by the Associations leading up to the agreement of September 1, 1980. To some extent the Stipulation went further, as in the provisions ensuring the independence of the Associations from CPG influence. However, it is obvious that the vigorous prosecution of these lawsuits was the principal cause, if not the sole cause, of the revisions in practices carried out by the Associations commencing in February 1979.

The Stipulation of Settlement contains certain additional terms relating to the disposition of the litigation. It was agreed that the plaintiff class would be expanded from insurance-buying members of AARP to all persons who were members of AARP or NRTA, as of November 1, 1980. This agreement was to apply to both the state and federal actions. NRTA was to be added as a defendant in both actions. Plaintiffs' counsel were to apply to the state court for fees and disbursements not exceeding $2.325 million, the first $1 million of which was to be paid 90% by CPG and 10% by the Associations, the excess over $1 million was to be paid 70% by CPG and 30% by the Associations. The agreement provided that defendants could withdraw from the settlement if more than 10,000 class members opted out of the class and sought monetary relief.

The Stipulation of Settlement contains a broad provisions barring claims by members of the class, either on behalf of the class or derivatively on behalf of the Associations.

In the state action, Peter Johnson was appointed referee to report on the fairness of the settlement agreement. Referee Johnson held hearings commencing in January 1981 and continuing through April 1981. On May 27, 1981 the referee filed his report recommending approval of the settlement and recommending an award of fee and disbursements of $2.325 million. The justice who will rule on the matter in the state court is Justice Israel Rubin. The matter is still under submission before him.

On June 19, 1981 the federal district court entered an order conditionally certifying the class as described in the Stipulation of Settlement. Notice of hearing on the settlement and fee application was given. Hearings were held, resulting in the ruling and judgment approving the settlement and approving the award of fee and disbursements in the amount of $2.325 million. The judgment was entered on September 10, 1982. This led to the appeal and the Second Circuit decision of May 2, 1983 remanding the matter for further consideration.

The plaintiff class, as originally defined, consisted of about 2.5 million persons. The plaintiff class as expanded by the Stipulation of Settlement consists of about 11 million persons. The number of persons who have opted out of the class is 2,850. The number of persons who have objected to the settlement is 11.

Discussion

Fairness of Settlement

As the concurring opinion of Judge Newman in the Court of Appeals points out:

> In this context the lawsuits were settled on

> terms that provide the plaintiffs with virtually all of the relief they sought in their complaints. The settlement proposes to secure in an enforceable consent judgment not only the contractual rights inuring to the Associations by virtue of their 1980 agreement with CPG, but also the very important additional requirement that the Associations will invite competitive bidding for the opportunity to provide health insurance for their members.

706 F.2d at 436

It is difficult to overstate the far-reaching results of this litigation and the settlement. Relationships between the Associations and CPG which had existed for more than 20 years came to an end. The value of those relationships is only partly indicated by the figure of $261 million for health insurance premiums paid by AARP/NRTA members in 1977, the year the federal action was commenced. It was hotly debated in the course of the litigation whether the arrangements between the Associations and CPG were as favorable to the Associations and their members as they should have been. However, one thing is clear. The attack mounted by plaintiffs succeeded. The Associations have broken virtually all ties to CPG, and group health insurance contracts and other business dealings are now dealt with by CPG on an open competitive basis. Prudential Insurance Company has replaced CPG as the group health insurer. Few class actions have ever succeeded in altering commercial relationships of such magnitude. Few class actions settlements have even approached the results achieved here.

The only question relating to the fairness of the settlement arises from the fact that damage claims were not

pleaded in either the state or the federal action, but that nevertheless they are sought to be barred in the settlement. Since we are only concerned with the federal action, the only damage claims which need to be dealt with are antitrust damage claims on behalf of the class and derivative antitrust claims on behalf of the Associations. It is the conclusion of the court that it was entirely fair and reasonable for the settlement agreement to provide that such damage claims would be barred.

As to the antitrust claims on behalf of the class, what is referred to is possible claims for premium "overcharges" under §§ 1 and 2 of the Sherman Act, 15 U.S.C.§§ 1 and 2. The relevant damage provision is contained in § 4 of the Clayton Act, 15 U.S.C.§ 15.

On the merits of these claims the issues fall into two categories. *First,* there are the issues relating to liability. In this regard, the same issues which pertain to the injunction claim would pertain to any claims for damages. *Second,* there are the damage issues themselves, particularly in regard to the difficulties of proof for so large a class.

In regard to liability, defendants presented a serious motion under § 2(b) of the McCarran-Ferguson Act, 15 U.S.C. § 1012(b). Aside from the issues raised on that motion, there were other substantial questions. With regard to Sherman Act § 1, we start with the proposition that there was nothing illegal about the Associations having an exclusive contract with one insurance company to provide group health insurance to the members. Plaintiffs' challenge under § 1 was to the relationship between CPG and the Associations which, in plaintiffs' view, prevented a selection procedure open to competition by other insurance companies. Plaintiffs claimed that this was an unreasonable restraint affecting a sufficient amount of commerce to constitute a violation of § 1. Defendants

contended that there was nothing unlawful about the selection procedure, but if there was, this was nothing but a breach of fiduciary duty under state law and not a § 1 violation. Defendants also contended that there was no restraint of trade of any significance. Among other things, defendants pointed to the fact that only one-fourth of the members of the Associations purchased health insurance from CPG, and that more members purchased such insurrance from other carriers than they did from CPG. As to the Sherman Act § 2 claim, it is sufficient to say that there is serious doubt about the ability of plaintiffs to demonstrate monopolization of a market in which numerous large insurers participate.

What has been said is a capsule description of the various factual and legal issues which would have been fought out if the federal court action had been litigated to the end. It is clear that the issues were difficult and that one cannot say with any degree of certainty what the outcome would have been. There was ample justification for a settlement.

It is worth returning now to a point noted earlier — the relationship of the state court action and the federal court action. As already described, the parties conducted their discovery in the state court action, and the various disputes about discovery were dealt with in the state court. Moreover, the submission of the settlement and the fee application was made in the first instance to the state court referee. In view of the numerous problems with plaintiffs' federal antitrust claims, it is reasonable to assume that the state court claims had a better chance of success than the federal court claims. In any event, the parties apparently viewed the state court as the more important situs of the litigation.

We now come to the damage issues. The federal action was commenced in 1977. If damages had been claimed, the four-year antitrust statute of limitations would have permitted claims going back to 1973. If we assume a trial in 1980 or thereafter and the filing of supplemental complaints, this would allow a total period of seven years or more for antitrust damage claims. As already noted, the expanded class as defined by the stipulation of settlement consists of 11 million persons. The number of insurance-buying members of the class (potential damage claimants) would be at least 2½ million and possibly substantially more. The measure of damages would be how much the claimant has been "injured in his business or property." 15 U.S.C. § 15. That amount would, of course, be trebled. The specific question on antitrust claims by members of the class would have been: How much more were they charged in premiums by CPG than they would have been charged by some other company, or by CPG, selected in an open competitive market?

During the relevant period there were 17 different AARP plans and 9 NRTA plans. These plans were amended at various times. It would have been necessary to determine whether a particular coverage could have been obtained at a lower price under different competitive conditions.

One can be reasonably sure that the trial of such claims would not have literally involved a separate hearing for each of the claimants. Undoubtedly, there could have been the formation of sub-classes. However, it would seem that the number of sub-classes would not be small, but would surely be some multiple of the number of plans (26).

Aside from the difficulties of proof, the various tasks involved in processing and administering the great number of potential claims would involve great effort and expense.

This brings us to the value of the claims. In terms of individual claims (and this is the only proper measurement) this would be minimal. Most of the premiums paid by AARP/NRTA members to CPG ran between $4.50 and $9.75 per month. The so-called "overcharges", if they could be proved at all, would be some relatively small percentage of these monthly premiums. One of plaintiffs' attorneys has estimated in an affidavit that the individual damage recoveries would likely be less than $100. There has never been any challenge to this estimate and it appears to be quite realistic.

One rough test of its validity appears from the following. Counsel for the Associations have advised the court that the new arrangement with Prudential involves a reduction of premiums on some policies, although on many policies the premiums are as before. Prudential has agreed to a fixed 75% loss ratio (the ratio of benefits to premiums), and has agreed to set aside any difference between that ratio and any lower ratio into a reserve fund for the future benefit of policyholders. In effect, what Prudential has done is to make a reduction in premiums to some policyholders, but largely await experience to see if there should be any broader reduction in premiums or any increase in benefits. In any event, the estimate is that, where premiums have been reduced, the reduction is about 10%.

No one believes that this 10% reduction is any appropriate measure of what antitrust damages would be for persons who bought insurance from CPG. However, it is perhaps some rough indication of the possible range of antitrust damage claims. For instance, if we assume that a person who was paying $9.00 per month would have been able to purchase from another company at 10% less – we have damages of $.90 per month. Trebled, that gives an

amount of $2.70 per month. This gives antitrust damages at the rate of $32.40 per year. If we realize that the 10% is probably generous, and that the $9.00 represents the higher end of the premiums, it becomes apparent that the antitrust damages, if they could be proved at all, would be something considerably less than $32.40 per year.

This is obviously a situation where the value of damage claims would be so small as to be virtually meaningless to the purported "beneficiaries." When the value of these claims is viewed in the context of the various questions of antitrust liability and the difficulties in proving damages and administering the claims, it becomes clear that it was sound judgment by plaintiffs not to assert them in the complaint, and it was salutary for the settlement to bar them, particularly in view of the outstanding results achieved in the settlement by way of prospective relief.

The statement in *Eisen v. Carlisle & Jacquelin*, 479 F.2d 1005, 1017 (2d Cir. 1973)[3], applies in the present case:

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[3]This decision was reviewed by the Supreme Court, which agreed with the Court of Appeals that the class action as defined in the complaint should be dismissed, although the Supreme Court opinion dealt only with the question of notice, and did not deal with the other points discussed in the Court of Appeals opinion. 417 U.S. 156 (1974). The literal order of the Supreme Court was:

> We therefore remand the cause with instructions to dismiss the class action as so defined.
>
> The judgment of the Court of Appeals is vacated and the cause remanded for proceedings consistent with this opinion.

417 U.S. at 179. Perhaps the reason for this order was that the Court of Appeals had dismissed the class action without prejudice to the action of the individual plaintiff (479 F.2d at 1020), whereas the Supreme Court dismissed the class action without prejudice to plaintiff moving to redefine the class (417 U.S. at 179 n. 16).

> The fact that the cost of obtaining proofs of claim by individual members of the class and processing such claims was such as to make it clear that the amounts payable to individual claimants would be so low as to be negligible also should have been enough of itself to warrant dismissal as a class action.[4]

The Court of Appeals in the present case suggests, however, certain alternative theories of damages for consideration. One of these is the possibility that "means may be available to assess the harm to the class even if proof of each of plaintiff's damages would be difficult." 706 F.2d at 435. With all due respect, it must be stated that this suggestion is not in accordance with the law of damages in antitrust cases.

Rule 23, providing for class actions, does not "abridge, enlarge or modify any substantive right." 28 U.S.C. § 2072. Rule 23 cannot be used as a device for departing from the statutory requirement that antitrust damages may be recovered only by a "person who shall be injured in his business or property" by reason of the antitrust violation. 15 U.S.C. § 15. The claims of many cannot be treated collectively or as the claim of "the class as a whole." *Eisen v Carlisle & Jacquelin, supra* at 1014, 1018. In *In re Hotel Telephone Charges,* 500 F.2d 86, 90 (9th Cir. 1974), the Ninth Circuit stated:

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[4]The present case is not, of course, being dismissed as a class action. The Stipulation of Settlement provides for class action certification and defines the class. For reasons stated later in this opinion, the court is of the view that this certification is appropriate and serves a valid purpose. But the question remains as to what are fair and reasonable terms for the settlement of the class action. The utility of the *Eisen* quotation, for purposes of the present case, is that it supports the view that waiver of potential damage claims is fair and reasonable in view of their minimal value.

> We agree with the decision reached in *Eisen v. Carlisle & Jacquelin* . . . that allowing gross damages by treating unsubstantiated claims of class members collectively significantly alters substantive rights under the antitrust statutes.

Another suggestion by the Court of Appeals in the present case is

> . . . the possibility that plaintiffs' loss could be measured as CPG's excess gain, *see Zeller v. Bogue Electric Manufacturing Corp.*, 476 F.2d 795, 802 (2d Cir.), *cert. denied,* 414 U.S. 908 (1973), a possibility that cannot be dismissed or simply overlooked in light of the statements in plaintiffs' counsels' affidavit that CPG's arrangement with the associations was very profitable, that "the opening of competitive bidding for the Associations' $270 million annual group health insurance has resulted in increasing the cash payout of group health insurance benefits to class members by over $39 million per annum" and that opening the associations' publications to other advertisers will increase advertising revenues by "over $19 million" in "the next five years alone."

706 F.2d at 435.

It should be noted that *Zeller* was neither a class action nor an antitrust case; it was a derivative action brought under the federal securities laws and certain common law theories. However, these distinctions, while of interest, are not crucial for present purposes. The Court of Appeals in *Malchman* cited *Zeller* for the theory of damages that a plaintiff's loss may at times be measured by a defendant's "excess gain." This is, of course, perfectly true. If a defendant has defrauded a plaintiff out of certain proper-

ty and has received that property, the plaintiff's damages may be equal to the defendant's gain; and there may be times when it is useful to measure the gain to the defendant in order to fix the amount of the plaintiff's damages. A situation such as this was discussed in *Zeller*. The claim there was that one corporation (Bogue) had improperly caused an affiliated corporation (Belco) to make a loan to Bogue at rates unduly favorable to Bogue. Thus it was claimed that Belco had lost the additional return which it could have earned by lending the money elsewhere, and Bogue had improperly benefited by obtaining the loan on the terms which were too favorable to it. The Court of Appeals discussed what it termed two theories of damages — the loss to Belco and the improper benefit to Bogue. The court stated that in practical effect, the second theory was "the mirror image of the first." 476 F.2d at 802. However, the court stressed the need for the plaintiff to prove that Belco could have found a borrower willing to pay a greater rate of interest than had been paid by Bogue. The dismissal of the case on motion was reversed.

Zeller authorizes no departure from the normal rule of damages in antitrust class actions. Indeed, the statement in *Zeller* about the plaintiff being required to prove availability of another borrower who would provide a greater return, is quite similar to what would be the necessity for the class claimants in the present case to show — *i.e.*, that they could have obtained their health insurance at more favorable rates from some other source under more competitive conditions.

The Court of Appeals in the present case also suggests that an increased "cash payout" to Association members of over $39 million per year, and increased advertising revenues to the Associations of over $19 million in the next five years, might provide measures of damages. The $19

million item will be discussed later in connection with possible derivative damages to the Associations. It has no bearing upon possible damage claims by class members. This leaves for discussion the $39 million item.

The fact is that this figure has virtually no bearing upon the question of antitrust damages by class claimants. As noted earlier, Prudential has committed itself to a loss ratio of 75%, and has agreed that any difference between this 75% loss ratio and any lower loss ratio which may occur will be put into a reserve fund for the benefit of policyholders. In attempting to quantify the benefit which would thus accrue to the policyholders, plaintiffs' counsel has estimated that the difference between the 75% Prudential loss ratio and an average CPG loss ratio in the past is 14.6%. Applying this percentage to a figure of $270 million, representing premiums paid by Association members in 1979, would produce a figure of $39 million.

There are several reasons why this calculation is of little or no use in dealing with the question of antitrust damages to class claimants. *First,* the purpose of the calculation is to try to convey an idea of the value of the *prospective* benefits to the class from the settlement. *Second,* although perhaps useful for this purpose, it is only the roughest kind of estimate even of such prospective benefits. As to what Prudential's loss ratio would be for the years after 1981, this remains to be seen. *Third,* whatever Prudential's loss ratio is in the years after 1981, there is no assurance whatever that this would be helpful in measuring what Association members would have paid in premiums in earlier years, going back to 1973, to Prudential or other companies under the competitive conditions which plaintiffs urge should have obtained. *Fourth,* it must be remembered that the antitrust laws do not provide for damages on an unjust enrichment theory. Injury to the

plaintiff's business or property must be proved. *In re Hotel Telephone Charges,* 500 F.2d 86, 92 (9th Cir. 1974); *Wilson P. Abraham Construction Corp. v. Texas Industries, Inc.* 604 F.2d 897, [illegible] n. 5 (5th Cir. 1979), *aff'd,* 451 U.S. 630 (1981), *Fifth* [illegible]e reference by the Court of Appeals in the *Malchman* opinion to the $39 million figure appears to be closely related to the suggestion of dealing with the "harm to the class." As already stated, this approach is contrary to the law of antitrust damages.

The Court of Appeals requested consideration of the case of *Copitka v. Colonial Penn Group, Inc.,* No. 442574 (Cal. Super. Ct., San Diego Cty., 1979). This was an action brought by an AARP member and his wife against CPG in a California state court under California law. The case is irrelevant to the issues in the present federal antitrust class action. The California case involved a claim that CPG improperly failed to reimburse more than a small percentage of certain large hospital bills. Compensatory and punitive damages were claimed. The case was settled for $500,000. The case did not involve claims for alleged overcharges in premiums.

Upon consideration of the matters referred to by the Court of Appeals in the present case, this court still concludes that it was entirely reasonable for the settlement agreement to bar damage claims on behalf of the class as part of the consideration for the settlement. One additional factor which should be noted is that only the smallest handful of persons has objected. Moreover, there has been ample opportunity for the objectors or the persons opting out to bring actions seeking antitrust damages. No such action has been brought.

The question of derivative damages can be dealt with briefly. This brings us back to the $19 million in advertis-

ing revenues referred to in the Court of Appeals opinion, as being an estimate of one of the benefits of the settlement over a period of five years. This, of course, refers to benefit to the Associations, and there is a suggestion that this is some measure of damage to the Associations caused by the alleged antitrust violations. Again, there has been ample opportunity for the objectors or the persons opting out to bring such a derivative action. None has been brought, and for good reason. Under New York Not-For-Profit Corporation Law § 623(a), a derivative action on behalf of associations such as these must be brought by at least 5% of any class of members. There is no indication that any such proportion of the members of the Associations has any interest in bringing such a derivative action.

Representation.

The Court of Appeals directed that the question of the adequacy of representation be further considered on remand.

Objectors contend that the named plaintiffs are inadequate representatives because of their relationship to class counsel. Plaintiff Nathan Malchman is the brother of class co-counsel Irving Malchman. Plaintiff Conway is the sister of the chauffeur of Milton Gould, a senior partner of Shea & Gould. Plaintiff Louis Stone is a personal friend of class co-counsel Stanley Kaufman. *See* 706 F.2d at 432.

There is some authority for the argument that a plaintiff who is a close relative of the attorney may be disqualified as a representative of the class. The theory is that such a relationship may result in an improper settlement. *See Susman v. Lincoln American Corp.*, 561 F.2d 86, 90-91 (7th Cir.1977). In that case class action status was denied

because plaintiff was the brother of the attorney. However in *Fischer v. ITT,* 72 F.R.D. 170 (E.D.N.Y.1976), the court allowed a class action to proceed where the plaintiff was the father of the attorney. The court analyzed the cases and found that the "touchstone" for denial of class action status was the question of whether the plaintiff had an interest in the attorney's fee.

There is no indication that any of the plaintiffs in the present litigation have an interest in the attorneys' fees or that plaintiffs have acted in any manner other than as normal and proper plaintiffs in a class action. Moreover, one of plaintiffs is William Deautriell, a former AARP chapter head, who has no relationship with any of plaintiffs' attorneys.

It is, of course, a matter of common experience in class actions that the named plaintiffs are often people of very little sophistication in financial or legal matters. It is almost always the attorneys who make the litigation decisions, determine strategy, and negotiate settlement terms. In practical fact, the quality of the attorneys is frequently the most important factor in determining the quality of representation. *See Shaffery v. Winters,* 72 F.R.D. 191, 193 (S.D.N.Y.1976).

In the present case, the attorneys representing the class have acted with outstanding vigor and dedication. When the litigation began, the class was represented by the firm of Kaufman, Taylor, Kimmel & Miller. The Kaufman firm brought in Shea, Gould to have the full litigating resources of a large firm. Shea, Gould was clearly not brought into the case for the purpose of achieving some quick settlement, but because of the desire to litigate these complex actions with all possible strength.

Although the lawyers in this litigation have appeared

considerably more in the state courts than in the federal court, they have appeared in the federal court sufficiently for me to attest as to the high professional character of their work. Every issue which has come to this court has been presented by both sides with a thoroughness and zeal which has been outstanding. There has never been the slightest hint in the conduct of plaintiffs' attorneys that they were willing to sacrifice legitimate claims for an easy settlement.

In considering the vigor of their representation, it must be recognized that plaintiffs' attorneys had the responsibility of determining what claims were worth pursuing and what were not. As described earlier, they sued for injunctive relief and not for damages. It is clear from the objective facts that this was a sound decision. When it came to the settlement agreement, it hardly needs to be said that a 100% victory on the claims sued upon speaks clearly for the vigor of the advocacy. For reasons already set forth, the agreement to waive damage claims gave up nothing of any substantial value.

Another point made by objectors is that, even if plaintiffs were capable of representing the class as originally defined, they cannot properly represent the class as expanded in the settlement agreement. As stated earlier, the class described in the original complaint consisted of those members of AARP who had purchased health insurance from CPG. At the time of the settlement it was agreed that the class would be expanded to include all AARP members (including those who had not purchased CPG insurance) as well as all NRTA members. A group called "AIM" was also included, but this was merely part of AARP.

With regard to the claims for injunctive relief, which were the subject matter of the actions, the interests of the

persons added to the class in the settlement were the same as the interests of the original class members. To the extent that it is beneficial to have the health insurance carrier selected by competitive bidding, this is beneficial to all members of AARP and NRTA.

It is true, of course, that the class was expanded in the settlement largely to give defendants the maximum protection against further litigation regarding the issues raised in these actions. This was a perfectly reasonable objective. It goes without saying that no purpose would be served by having further litigation on the claims for injunctive relief, in view of what was achieved in the settlement. As to possible damage claims by the class members, the class as originally defined had a *greater* interest in such claims than most of the new class members, and could fairly waive these claims without incurring any conflict with the new class members (most of whom had no damage claims to waive, since they had not purchased insurance from CPG). As to derivative claims, the interests of all members of AARP and NRTA were identical, and plaintiffs could fairly represent all these persons in the settlement.

Fee Application.

The Stipulation of Settlement provides that plaintiffs' attorneys would apply for approval of fee and disbursements not to exceed $2.325 million and that defendants would not oppose such an application. It was further agreed that of the first $1 million awarded, CPG would pay 90% and the Association would pay 10%, and of any remaining award, CPG would pay 70% and the Associations 30%. If the full $2.325 million is awarded, CPG will pay $1,827,500 and the Associations will pay $497,500.

Certain circumstances should be noted at the outset. It

is of some significance that the bulk of the fee will be paid by CPG. This does not mean that such a payment is beyond the scrutiny of the court. However, the payment by CPG to plaintiffs' attorneys is not being deducted from any settlement fund payable to the class, nor do the circumstances suggest any collusion by CPG and plaintiffs' attorneys to arrange for an improper settlement. Even if one were to consider that the amount being paid by CPG constituted some kind of a settlement fund, it would amount to only a few cents per class member. It should also be kept in mind that the fee application is made both to the federal and the state courts. Approval of the $2.325 million fee request has been recommended by the state court referee. It would seem clear that the orderly administration of justice would require that some deference be given to the proceedings in the state court. Most of the attorneys' work was carried out in the state court action. Also, for reasons already stated, the parties appear to have regarded the state court as the more important situs of the litigation.

Nevertheless, the Court of Appeals has directed that an independent review be made in the federal court regarding the fee application. This has been done. The $2.325 million applied for includes $2,085,901 for fee and $239,098 for disbursements and paralegal expenses. The time records for Shea & Gould and Kaufman Malchman & Kirby show a total of 10,282.75 hours spent on this litigation through August 31, 1981. The great bulk of this time was spent prior to the settlement agreement of November 3, 1980, although a modest amount of time (945 hours) was spent in proceedings thereafter relating to submission of the settlement and the fee application to the state and federal courts. At Shea & Gould, most of the partner time was spent by Michael Lesch. His normal hourly rate dur-

ing the time of the litigation was $135-150. At the Kaufman Malchman firm, substantial amounts of time were spent by Stanley L. Kaufman and Irving Malchman, whose hourly rates were $200 and $150 respectively. At Shea & Gould there were a few other partners besides Mr. Lesch, and a number of associates, who worked on the case. The hourly rates for the attorneys at these firms, both partners and associates, are entirely reasonable. The amount arrived at by taking the number of hours multiplied by the normal hourly rates is $1,237,412. The fee requested ($2,085,901) is 1.685 times $1,237,412.

Objectors have singled out three instances of what they claim was wasted or duplicated effort. These involve a relatively small number of hours, and the criticisms are unwarranted. Objectors also contend that there should be no allowance for a total of about 1,150 hours spent after May 1, 1980 when it is alleged that the "agreement in principle" to settle was reached. However, the record shows that negotiations and other work, normally used as a basis for a fee application in a class action, continued after the May 1, 1980 date.

Even if all the time complained about by objectors is taken out, the number of hours multiplied by the regular rates would equal about $1 million. Based on this amount, the multiplier necessary to arrive at the requested fee of $2,085,901 is 2 and a small fraction.

Either the multiplier of 1.685 or the multiplier of 2 is well within what has been used in connection with antitrust class action fee awards. *See, e.g., In re Gas Meters Antitrust Litigation,* 500 F.Supp. 956 (E.D.Pa.1980) (multiplier of two and one half); *In re Gypsum Antitrust Cases,* 1974-2 Trade Cases (C.C.H.) ¶ 75,272 (N.D.Cal. 1974), *aff'd,* 565 F.2d 1123 (9th Cir. 1977) (multiplier of three).

The Court of Appeals asked six questions (706 F.2d at 435-36), the answers to which should be clear from what has been stated. Nevertheless, they will be specifically addressed.

> Why was a bonus awarded so large as to produce a total fee award that amounts to double the usual rates for counsel – for a total of approximately $240 per hour – regardless of the difficulty of the tasks performed?
>
> What difficulty was involved that was extraordinary?

The average hourly rate before applying the multiplier is $120. An examination of the time records shows that a large number of hours was spent, but the amount of work was not unreasonable in view of the scope and complexity of the litigation. Moreover, it appears that the tasks were apportioned among various attorneys of various degrees of seniority in the normal way – according to the difficulty of the particular project. Shea & Gould spent the greater amount of time – 6,440.50 hours versus 3,842.25 hours for the Kaufman firm. Shea & Gould had a number of associates available to work at relatively low rates.

As to the size of the multiplier or bonus, it should be noted at the outset that the $240 figure referred to by the Court of Appeals appears to be incorrect. If the requested fee ($2,085,901) is divided by the number of hours (10,282.75) this gives an average rate of $203 per hour. More important, the multiplier of 1.685 would appear to be amply justified in light of the applicable standards. *See City of Detroit v. Grinnell Corp.*, 495 F.2d 448, 470 (2d Cir.1974).

This litigation was of unusual importance and magnitude, for the reasons already pointed out. As to the complexity of the issues, it would be inappropriate for the

federal court to inquire into the degree of complexity of the state court issues. As to the federal antitrust issues, it is clear that they were numerous and complex. There was no prior judgment or decree in a Government case upon which plaintiffs could rely.

In sum, plaintiffs and their attorneys undertook a very large and difficult litigation in both the state and federal courts, where the stakes were enormous. This litigation was hard fought over a period of four years. Plaintiffs achieved a settlement which altered commercial relationships involving literally hundreds of millions of dollars. The multiplier of 1.685 and the requested $2,085,901 for fees are modest in view of all the circumstances. One of the factors justifying such a multiplier is the large investment of attorney labor without payment since 1976.

The next question of the Court of Appeals is:

> Why was all the time necessary for the mere pursuit of injunctive relief to which there was such rapid agreement in principle?

The answer is that there was no "rapid agreement in principle." The chronology of the litigation makes this clear.

The Court of Appeals further asks:

> Was the recital of the draft proposal of defendants to the effect that plaintiffs' counsel had researched the legal principles applied to damage claims dropped in the executed stipulation and, if so, why?

The answer is that the recital was not dropped. Paragraph O of the Stipulation of Settlement provides:

> Additionally, plaintiffs' counsel have studied the applicable legal principles underlying this litigation (including, but not limited to, the legal prin-

ciples that would govern any possible damage claims and the assertion of such damage claims in a class action).

Another question is:

> Were the fees agreed upon before the settlement was reached or only after substantive issues were worked out?

It has been averred in affidavits by Michael Lesch, co-counsel for plaintiffs, Sidney Rosdeitcher, attorney for CPG, and Geoffrey Kalmus, attorney for the Associations, that the amount of the fee application was not negotiated or agreed upon until after the main substantive terms of the settlement were arrived at. These averments, viewed in the light of all the circumstances, appear entirely credible.

The final question asked by the Court of Appeals was:

> Why were the associations to pay any part of the bill since the gravamen of the complaints was that the associations (or their members) had lost money by virtue of CPG's actions?

It is settled law that attorneys' fees may be charged against the beneficiary of a class action. *See Kopet v. Esquire Realty Co.*, 523 F.2d 1005, 1008 (2d Cir.1975). In the present case, affidavits from the Associations make it clear that they were desirous of ending the litigation, because it was interfering with the conduct of the business of the Associations and was a cloud on their reputations. Their agreement to a modest contribution toward the attorneys' fees was entirely reasonable and lawful.

One further point should be dealt with, which bears upon the fee application as well as the fairness of the set-

tlement. The Court of Appeals referred to what it termed "the CPG defendants' quick capitulation," 706 F.2d at 435, and appended the following footnote:

> 5. We do not intend to imply that quick settlements should be viewed with heightened suspicion; few cases will seek to dispose of the rights of so many persons who are not active participants in a suit on the basis of as little vigorous presettlement investigation of the merits of their claims as this one.

It is only just to say that these statements are inaccurate. The record demonstrates without question that there was a long and conscientious struggle by the attorneys for both plaintiffs and defendants to achieve an honorable and realistic disposition of this important case.

For the above reasons this court approves the application of plaintiffs' attorneys for an award of a fee in the amount of $2,085,901 and disbursements and paralegal expenses in the amount of $239,098 or a total of $2.325 million.

Discovery.

Objectors have contended, since the time of the remand, that they should be allowed to engage in discovery. However, such discovery is not warranted where the court has sufficient materials already before it to evaluate the settlement and fee application, and where the objectors have failed to make cogent factual objections which indicate the need for discovery and a possible evidentiary hearing. *See Weinberger v. Kendrick,* 698 F.2d 61, 74, 79 (2d Cir. 1982), *cert denied,* ____ U.S. ____, 104 S.Ct. 77 (1983). In the present case, a large record exists which is ample to

permit decision on the relevant issues. There is no reason for permitting objectors to engage in discovery.

Conclusion

This court approves the Stipulation of Settlement of this action, including the request by plaintiffs' attorneys for an award of attorneys' fee and disbursements of $2.325 million.

So ordered.

APPENDIX C

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

No. 888—August Term, 1982

(Argued February 14, 1983 Decided May 2, 1983)

Docket No. 82-7759

NATHAN MALCHMAN, GERTA CONWAY, WILLIAM DEAUTRIELL, and LOUIS STONE,

Plaintiffs-Appellees,

—v.—

LEONARD DAVIS, SOPHIE DAVIS, COLONIAL PENN GROUP, INC., COLONIAL PENN FRANKLIN INSURANCE COMPANY, INTRAMERICA LIFE INSURANCE COMPANY, NATIONAL ASSOCIATION PLANS, INC., AMERICAN ASSOCIATION OF RETIRED PERSONS, NATIONAL RETIRED TEACHERS ASSOCIATION, CARRIE B. ALLEN, ORANDA BANGSBERG, BERNARD BERGGREN, JUNE BIGGAR, ARTHUR BOUTON, OLAF KAASA, CLARA L. KLEWENO, FLOYD E. TUMBLESON, J. LEONARD JOHNSON, C. E. CARMICHAEL, AMERICAN ASSOCIATION OF RETIRED PERSONS INSURANCE TRUST, DOROTHY M. CRIPPEN, JAMES J. BROWNING, LLOYD I. SINGER, CYRIL F. BRICKFIELD, and JOHN J. MACWILLIAMS,

Defendants-Appellees,

MOUNTAIN PLAINS CONGRESS OF SENIOR ORGANIZATIONS, MR. AND MRS. HUGH A. GROVES, FRANCIS SEELY,

ESTELLE WHITTLE, HENRY WHITTLE, MR. AND MRS. BURTON W. ATKINSON, MR. AND MRS. C. E. DIETRICH, HARRIET MILLER, and ALICE VAN LANDINGHAM,

Objectors-Appellants.

Before:

LUMBARD, OAKES, and NEWMAN,

Circuit Judges.

Appeal from approval of settlement by the United States District Court for the Southern District of New York, Thomas P. Griesa, *Judge,* in class action suit for federal antitrust violations.

Reversed and remanded.

JOSEPH A. YABLONSKI, Washington, DC (Daniel B. Edelman, Yablonski, Both & Edelman, Washington, DC; Philip J. Hirschkop, Hirschkop & Grad, P.C., A'exandria, VA; Robert J. Sugarman, Sugarman & Denworth, Philadelphia, PA), *for Objectors-Appellants.*

MICHAEL LESCH, New York, NY (Fran M. Jacobs, Shea & Gould, New York, NY; Stanley L. Kaufman, Irving Malchman, Kaufman, Malchman & Kirby, New York, NY, of counsel), *for Plaintiffs-Appellees.*

SIDNEY ROSDEITCHER, Washington, DC (Jeffrey C. Slade, Paul, Weiss, Rifkind, Wharton & Garrison, Washington, DC, of counsel), *for Colonial Penn Group, Inc., and related Defendants-Appellees.*

GEOFFREY M. KALMUS, New York, NY (Michael S. Oberman, Kramer, Levin, Nessen, Kamin & Soll, New York, NY, of counsel), *for Association Defendants-Appellees.*

OAKES, *Circuit Judge*:

This appeal is by objectors to the settlement of a class action antitrust suit. The settlement, while giving certain injunctive relief against some of the defendants, also waives any claim for damages for the defendants' past conduct by several million members of the plaintiffs' class(es). Coordinately, the settlement agreement covers a state court lawsuit for breach of fiduciary duty and conflict of interest arising out of the same facts. The settlement awards counsel fees and expenses totaling $2,325,000 for the two law firms representing the plaintiffs. The settlement was approved by the United States District Court for the Southern District of New York, Thomas P. Griesa, Judge, after a hearing and in an order which stated conclusions but made no specific findings. Our duty to review this important settlement cannot properly be fulfilled because we do not have sufficient analysis of several pivotal issues. We are required to remand this case for further consideration.

BACKGROUND FACTS

This litigation and the companion state court action, *Conway v. Davis*, No. 10535/76 (N.Y. Sup. Ct., N.Y. Cty.), principally arise from the relationship between Leonard Davis and various corporate entities owned or controlled by him and two nonprofit organizations of elderly persons, the National Retired Teachers Association (NRTA) and the American Association of Retired Persons (AARP).

Dr. Ethel Percy Andrus, a retired California high school principal, founded the NRTA in 1947 to promote the interests of retired teachers. In 1956, at Dr. Andrus's request, insurance broker Leonard Davis persuaded a national insurance company to underwrite a voluntary group health insurance program for the members of NRTA. In 1958, again with Davis's help, Dr. Andrus formed the AARP to serve the interests of Americans over 55 years old. AARP offered voluntary group health insurance to its members similar to NRTA's. Since their founding, the two associations have attracted millions of members and presently have, between them, over 13 million members throughout the United States. Meanwhile, Davis formed the companies that in time became Colonial Penn Group (CPG) to underwrite health insurance policies in group plans and to provide other services to the associations' members. From 1958 on Davis and his companies managed the AARP and NRTA insurance plans. The associations encouraged their members to purchase insurance, travel and other products and services exclusively through Davis-controlled entities, including insurance subsidiaries, group travel companies, and employment agencies. Davis's entities, moreover, had the exclusive right to advertise in the associations' publica-

tions and were permitted to do so at what appears to be substantially less than the fair market value of such advertising. CPG also maintained the membership lists of the associations in its computers.

As AARP and NRTA grew, so did Colonial Penn and its various subsidiaries, its total revenues being $171 million in 1972 and $445 million in 1976. The AARP/NRTA health insurance plans generated over $261 million in premiums in 1977. As of January 1, 1976, CPG led 929 major United States corporations in profitability with a five-year average annual return on capital of 33.5%, a figure nearly double the profitability of either IBM or Xerox and three times greater than the median return of 11.3% for the entire insurance industry.

THE STATE COURT LITIGATION

Lederer v. Colonial Penn Group, the original state court complaint, dated May 4, 1976, was a class action on behalf of insurance-buying members of AARP and alleged principally that the class was overcharged for insurance policies purchased from CPG. The complaint charged the defendants including Davis, CPG, and various people connected with the associations with fraud and breach of fiduciary duty. The complaint sought only injunctive relief and no damages. The action was brought by a firm known as Kaufman, Taylor, Kimmel & Miller (Kaufman-Kimmel). When a motion to dismiss was scheduled for oral argument, Shea & Gould, then known as Shea, Gould, Climenko & Casey, appeared as co-counsel for the plaintiffs and the original complaint was dismissed upon consent with leave to replead.

In July 1977, an amended complaint was served and filed in New York State Supreme Court with Gerta C.

Conway as an additional plaintiff. The amended complaint also alleged fraud and breach of fiduciary duties to AARP members who then held group health insurance, approximately 2.5 million persons. Defendants were Davis and his wife, controlling stockholders of CPG, CPG's chairman, AARP, members of its board and trustees of its insurance trust, and AARP's attorneys. Defendants moved to dismiss the amended state complaint.

The defendants took the initiative in the litigation, serving the plaintiffs with interrogatories and requests for production of documents. The defendants vigorously attacked the adequacy of the named plaintiffs as class representatives: each plaintiff was deposed and interrogatories were answered. Though plaintiffs did take a lengthy deposition of Harriet Miller, a former Executive Director of AARP who had filed a separate suit against Leonard Davis and others following her discharge, and thirteen other depositions, the plaintiffs never served interrogatories on any of the defendants or requested admissions from any of them in the state case. When plaintiffs served defendants with requests for production of documents in July 1978, defendants sought an order preserving confidentiality. As of early 1979, plaintiffs had obtained little or no discovery information from defendants. A stipulation of settlement was entered into on November 3, 1980, covering both the state court and the federal actions. That stipulation will be discussed in further detail below.

THE FEDERAL LITIGATION

This action, alleging violation of the federal antitrust laws, was filed by both the Shea & Gould and the Kaufman-Kimmel firms in October 1977 on behalf of

plaintiffs Lederer, Conway, and Nathan Malchman. This suit was also filed as a class action only on behalf of insurance-buying members of AARP and named essentially the same defendants as did the state court action. Like the state court action it sought injunctive relief and not restitution or money damages. No discovery at all was undertaken by plaintiffs in this action. In September of 1980, CPG and the associations made an agreement including the following provisions: (1) the associations would select a group health insurance carrier commencing July 1, 1981; (2) the associations would accept advertising from companies other than CPG in their publications; (3) the associations would significantly revise their operating procedures thereby granting—indeed, granting—authority to the associations' boards of directors to select and supervise the associations' insurance plans, an assertion of independence in keeping with the associations' unilateral decisions to limit the rights of Honorary Presidents including Leonard Davis and to eliminate the provisions for the continuation of the trustees of the associations' insurance trust in office for life with the right to designate their own successors; (4) CPG would pay the associations a total of $6,866,664 and would spend not less than an additional $4.5 million to promote membership in the associations during the period January 1, 1980, through June 30, 1981; (5) CPG would transfer the custody and maintenance of the associations' membership lists to the associations; (6) CPG would no longer engage in Chapter activities; (7) CPG could no longer claim association endorsement for its products without permission; and (8) CPG was barred from advertising in CPG publications if another underwriter was selected.

Neither the defendants' motion to dismiss nor class certification had been acted upon when the parties pre-

sented the district court with the stipulation of settlement on November 6, 1980. The stipulation of settlement was filed with an affidavit of Michael Lesch, Esq., the Shea & Gould attorney for the plaintiffs, and a number of other documents, including the September 1980 agreement entered into by CPG and the associations. The bulk of the stipulation of settlement primarily confirmed the arrangements in the September 1980 agreement but added the following terms:

1. Competitive bidding procedures for the placing of insurance by the associations were agreed upon as was an eight-year period of duration for the consent decree and a five-year period for the duration of the group insurance contract placed in 1981 with Prudential Insurance Co.;

2. Complete and final termination of both state and federal actions;

3. Amendment of the state and federal complaints to include NRTA as a defendant and to broaden the plaintiff class to all persons who as of November 1, 1980, were members of either AARP or NRTA;

4. Defendants' consent to the certification of the broadened class in both the state and federal actions, with plaintiffs' counsel to apply for entry of a consent order accomplishing the foregoing and appointing a referee (a) to inquire into and report on the fairness, adequacy, and reasonableness of the settlement, (b) to recommend the form of notice to the intended plaintiff class, and (c) to review and make recommendation of an application by plaintiffs' counsel for an award of attorneys' fees;

5. If the referee did approve the foregoing, plaintiffs' counsel was to seek a state supreme court order in effect confirming the referee's report and then seek a consent

order in the federal action accomplishing all of the foregoing there (except the attorneys' fees which were only to be sought in state court);

6. The associations were to make available space in one issue each of their news bulletins and an NRTA magazine to give notice of the settlement and the state supreme court hearing (the parties agreeing that such notice constituted "sufficient notice to the members of the intended plaintiff class");

7. Plaintiffs' counsel were to apply to the state supreme court for a total fee, including disbursements, not in excess of $2.325 million, the first $1 million of which CPG was to pay 90% and the associations to pay 10%, and of anything over $1 million CPG was to pay 70% and the associations were to pay 30%, and defendants not to oppose any such application;

8. The stipulation provided the defendants an escape clause in the event that more than 10,000 class members opted out of the class and sought monetary relief or if the settlement were disapproved by the state supreme or the federal district court or were disapproved upon any appeal from either or both such courts. (In this connection we note that any opting-out member up to 10,000 would thus still retain any benefits accruing as a result of the stipulations).

Thereafter, on June 19, 1981, an order was filed providing for class certification and the complaint was amended, adding the NRTA as a defendant and broadening the class of plaintiffs from insurance-buying members of the AARP to include the members of Action for an Independent Maturity (AIM) (an additional 300,000 persons), the members of the NRTA (an additional 500,000 persons) and non-insurance-buying members of the

AARP (an additional 10.5 million persons). The class in the settlement was four and one-half times larger than any that had been a party to the litigation up to that point.

PROCEEDINGS AFTER THE STIPULATION OF SETTLEMENT

The proposed settlement proceeded like clockwork except that the objectors-appellants who have taken an appeal here protested the settlement before the referee, Peter James Johnson, who was appointed on November 21, 1980, to inquire into the fairness, adequacy, and reasonableness of the settlement, the form and method of notice proposed to be given to the class, and the attorneys' fees. Hearings were held, exhibits were received, and pretrial discovery material including deposition transcripts and documents marked at depositions were received. The report summarized the stipulation as making five major changes in the relationship between CPG and the associations: (1) competitive bidding for insurance; (2) opening association publications to general advertising; (3) changing the self-perpetuation of the trustees of the insurance trusts and restricting the influence of the associations' honorary presidents; (4) transferring from CPG to the associations functions previously performed by CPG, including promotion of new memberships and maintenance of the associations' membership lists; and (5) termination of exclusive endorsements by the associations of CPG's non-health insurance products and services, including life, automobile, homeowner, and other insurance and travel services. For practical purposes, most if not all, as we have noted, had previously been accomplished by the September 1980 agreement.

The referee found that the settlement was conducted at arm's length and was fair, adequate, and reasonable. He noted that "substantially all the aims contemplated by the relief requested in the amended complaint" were accomplished by the settlement without the "enormous expense of a trial, and the cost of anticipated appeals." The report noted that the plaintiffs' litigation position was vulnerable and that the law was unsettled where members of the class have received substantial benefits and proof of individual claims would "probably be extremely difficult because of the variations in individual coverage and premiums paid." Despite these hardships, however, two members of the AARP who had purchased AARP-endorsed group health insurance underwritten by CPG had received $500,000 in settlement of a claim for compensatory and punitive damages in a California Superior court case, *Copitka v. Colonial Penn Group, Inc.*, No. 442574 (Cal. Super. Ct., San Diego Cty., 1979). *Copitka* was regarded as irrelevant to the possible success of a suit commenced under New York law because of California's unique punitive damage laws. The referee did not, however, explicitly consider the possible success of damage claims commenced in states other than New York, including California, and despite his view of the irrelevance of *Copitka* explicitly required disclosure of the *Copitka* settlement in the notice distributed to the class members through the associations' publications. He approved the application for attorneys' fees of $2.325 million, an amount approximately twice normal hourly rates for the participating attorneys and paralegals. The settling parties, in short, received from the referee everything that the stipulation had sought, with modification only in respect to the language of the notice to be given to the members of the now-to-be-expanded class of plaintiffs whose damage claims would be waived.

In accordance with the stipulation of settlement, plaintiffs' counsel applied to the federal court to enforce the settlement as approved by the referee. On June 19, 1981, the district court entered an order conditionally certifying the class and directing that notice of settlement be given and fixed a date for a hearing on the fairness, reasonableness, and adequacy of the settlement and directed that the hearing date be included in the notice. The fairness hearing was held on December 16, 1981. It consisted solely of a lawyers'/judge's colloquy, in the course of which the judge stated that he would review the attorneys' fee award, a matter in which plaintiffs' counsel quickly concurred. The hearing was adjourned so that Judge Griesa could review the papers filed in support of and in opposition to the settlement. At a subsequent hearing on August 4, 1982, Judge Griesa declared that he agreed completely with the findings of the state court referee as to the fee and entered an order accordingly.[1] The order did nothing more than in conclusory terms approve the settlement as above spelled out; no factual findings were made except that the state court referee's findings were incorporated in effect by implication. While hearings have been held, state Supreme Court Justice Rubin has not as yet approved the settlement.

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[1] Judge Griesa said at the conclusion of this colloquy:

> I have no reason to make any ruling or recommendation or take any action which would be contrary to what has been recommended by the referee in the State Court. I think that concludes these proceedings as far as the fee application.
>
> As far as the settlement, I agree completely with the findings of the referee as far as the fairness and adequacy of the settlement, and I have no reason for an extensive statement. The considerations are very thoroughly laid out by the referee. He summarizes the settlement and the problems, the objections that have been raised and deals with them. So I think that concludes my proceedings.
>
> What further paperwork has to be done?

OBJECTIONS TO THE SETTLEMENT

Appellants have raised six primary objections[2] to the settlement. First, they object to the adequacy of the plaintiffs-appellees as class representatives, pointing out that, even as to the class that they originally sought to represent, insurance-buying members of AARP, the named plaintiffs had interests antagonistic to those of the class: plaintiff Malchman was the brother of class counsel; plaintiff Conway was the sister of the chauffeur of class counsel, plaintiff Lederer was the mother-in-law of class counsel, and plaintiff Stone was a close personal friend of class counsel. Second, the named plaintiffs could not be adequate representatives of the larger classes ultimately certified pursuant to the terms of the settlement, classes which included NRTA and AIM members as well as non-insurance buying AARP members. Third, contrary to Rule 23 and the decisions of this and other courts, e.g., *Plummer v. Chemical Bank*, 668 F.2d 654 (2d Cir. 1982), the district court did not hold a proper reasonableness and fairness hearing and specifically failed to give proper weight to claims for money damages that

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2 Plaintiffs-appellees object to the objectors. They argue that objector Harriet Miller is a disgruntled former employee who is carrying on a personal vendetta; that attorney Yablonski's fees and disbursements were being paid by a third person whose identity has not been disclosed so that "the real party in interest behind these" objectors is this undisclosed third person; and that the objector Mountain Plains Congress receives money from the National Council for Senior Citizens which is said to be an arch-rival of AARP and NRTA and whose interest is said to be to continue to embroil the associations in litigation. However, even taking all these claims of the brief as true, so far as appears all of the named individuals objecting are members of the broadened class who have standing to object. We do not understand that the claim is made, or if it were that there is record support for it, that the undisclosed third person is paying fees and disbursements for all the objectors.

could have been made or to the fact that the relief obtained in the settlement had already been obtained by the extrajudicial agreement among the defendants dated September 1980. Fourth, in a case such as this where the district court gave approval of a tentative class certification purely for settlement purposes, the rule is that a "court must be doubly careful in evaluating the fairness of the settlement," *Plummer*, 668 F.2d at 657, a call for careful scrutiny that the district court did not heed in perfunctorily approving the settlement. Fifth, no evidentiary foundation was laid within *Plummer*, 668 F.2d at 659, so as to permit intelligent review. Rather, the district court simply relied upon the state court referee's findings and report, which itself gives inadequate consideration to various objections made. Finally, the district court deferred to the state court on the question of fees, contrary to Rule 23, and inappropriately permitted fee discussions to take place and agreement on the fee to be reached before all substantive issues affecting the class had been resolved. *See Prandini v. National Tea Co.*, 557 F.2d 1015, 1020 (3d Cir. 1977).

The objectors-appellants would have us direct the district court to decertify the class and to disapprove of the settlement.

THE ANSWERS OF THE SETTLING PARTIES

In addition to claiming that the objecting parties are entitled to no credibility because they have undisclosed and ulterior reasons for opposing the settlement, *see* note 2 *supra*, the appellees argue that the district court did not abuse its discretion, that it properly relied upon the state court referee, and that the settlement is fair and equitable. They argue that at least two of the named plaintiffs

have no obviously disqualifying characteristics, and that neither direct nor derivative monetary claims would have been maintainable, partly because the cost of notice to such large members of the class would be too great, partly because the measurement of insurance claims would present complex problems of proof of damages with minimal claims on the part of any individual class members. The settling parties argue that although the litigation has been pending for several years and although the California *Copitka* case was settled,[3] no other members of the associations have come forth to assert their individual claims. They add that the derivative claims are valueless because the associations benefited enormously from their relationship with Colonial Penn. Moreover, CPG points to the million dollars a year it paid for advertising in the associations' publications and points to the benefit to the associations from CPG's efforts to increase association membership.

The settling parties remind us that "the settlement provides for substantially all the relief [initially] sought in the action." Plaintiffs-Appellees' Brief at 37. They argue furthermore that the basic substance of the settlement was agreed to at the very outset of negotiations, well before the plaintiffs' attorneys' fee was considered. After the initial agreement counsel only sought to find the best mechanism for accomplishing the agreement. Interest-

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3 The *Copitka* suit was filed in 1979 and was settled by CPG for $500,000 on the eve of trial in March, 1981. Appellees claim this settlement was made because it was right at a time when CPG was attempting to persuade members of the existing group of AARP and NRTA to remain with it rather than to go with Prudential Insurance Co. which was awarded the associations' health insurance from and after July 1, 1981, in accordance with the the competitive bidding procedures of the September 1980 agreement. CPG was afraid of the "publicity attendant upon the trial."

ingly, they do not tell us how, if that was the case, the attorneys' fees awarded were justified.

DISCUSSION

We agree with objectors-appellants that we cannot intelligently review the settlement on this record and therefore must remand for findings.

There is no doubt that the district court must make an independent evaluation of whether the named plaintiffs were adequate representatives of the class of AARP insurance buyers they purported to represent at the time suit was brought, as well as of the broadened class ultimately approved by the order approving the settlement. Fed. R. Civ. P. 23(a)(4). Not only must the court examine whether plaintiffs had interests antagonistic to those of other class members, *Eisen v. Carlisle & Jacquelin*, 391 F.2d 555, 562-63 (2d Cir. 1968), *vacated and remanded on other grounds*, 417 U.S. 156 (1974), but also whether the class representative "possess[ed] the same interest and suffer[ed] the same injury" as the class members. *Schlesinger v. Reservists Committee to Stop the War*, 418 U.S. 208, 216 (1974). A judge has an obligation to consider whether the interests of the class are adequately represented, *see East Texas Motor Freight System, Inc. v. Rodriguez*, 431 U.S. 395, 403-06 (1977); *Plummer v. Chemical Bank*, 668 F.2d at 659 & n.4, and the court must examine the quality of representation with particular care where, as here, a class is sought to be broadly expanded after the litigation has been in process and for purposes of settlement, Fed. R. Civ. P. 23(c)(1). If the judge is not preliminarily satisfied that class members have been adequately represented in settlement nego-

tiations, he has the power and the obligation to explore the issue before approving the settlement.

The same principles are applicable to the issues of adequacy, fairness and reasonableness of the settlement, approval of which is required by Fed. R. Civ. P. 23(e) and the case law. *See, e.g., In re Traffic Executive Association—Eastern Railroads*, 627 F.2d at 633-34; *Greenfield v. Villager Industries, Inc.*, 483 F.2d 824, 833 (3d Cir. 1973). We have previously held that, while we do not expect the district judges to convert settlement hearings into mini-trials on the merits, we do expect them to explore the facts sufficiently to make intelligent determinations of adequacy and fairness, *Plummer*, 668 F.2d at 659; *see also In re Traffic Executive Association—Eastern Railroads*, 627 F.2d 631, 633 (2d Cir. 1980), and we have strongly hinted that making findings of fact and conclusions of law whenever the propriety of the settlement is seriously in dispute is desirable. *Plummer*, 668 F.2d at 659. The trial judge determines fairness, reasonableness, and adequacy of a proposed settlement by considering (1) the substantive terms of the settlement compared to the likely result of a trial, *Protective Committee for Independent Stockholders of TMT Trailer Ferry, Inc. v. Anderson*, 390 U.S. 414, 424-25 (1968); *In re Traffic Executive Association—Eastern Railroads*, 627 F.2d at 633, and (2) the negotiating process, examined in light of the experience of counsel, the vigor with which the case was prosecuted, and the coercion or collusion that may have marred the negotiations themselves. *Weinberger v. Kendrick*, 698 F.2d 61, 73 (2d Cir. 1982); *City of Detroit v. Grinnell Corp.*, 495 F.2d 448, 465 (2d Cir. 1974) (*Grinnell I*). *Grinnell I* sets forth the following as relevant factors in determining fairness of a settlement:

> (1) the complexity, expense and likely duration of the litigation, (2) the reaction of the class to the settlement, (3) the stage of the proceedings and the amount of discovery completed, (4) the risks of establishing liability, (5) the risks of establishing damages, (6) the risks of maintaining the class action through the trial, (7) the ability of the defendants to withstand a greater judgment, (8) the range of reasonableness of the settlement fund in light of the best possible recovery, (9) the range of reasonableness of the settlement fund to a possible recovery in light of all the attendant risks of litigation[.]

Robertson v. National Basketball Ass'n, 556 F.2d 682, 684 n.1 (2d Cir. 1977) (citing *Grinnell I*, 495 F.2d at 463). These are factual questions for the district court, *Plummer*, 668 F.2d at 659, and "a district court's disposition of a proposed class action settlement should be accorded considerable deference," *Weinberger*, 698 F.2d at 73; *see also In re Corrugated Container Antitrust Litigation*, 643 F.2d 195, 207 (5th Cir. 1981), *cert. denied*, 50 U.S.L.W. 3935 (U.S. May 25, 1982), though this principle applies with less force when, as here, settlement of a class action has been negotiated before the class has been certified. *Weinberger, supra*, at 73. The court's discussion need not be prolix to be thorough, and this court will affirm if its review of the record shows that the court "had before it sufficient materials to evaluate the settlement and came to the correct conclusion." *Weinberger*, 698 F.2d at 74 (parties' affidavits bearing on litigation history and evidence, discovery materials, and bankruptcy opinions provided satisfactory record). And if the record is adequate, an evidentiary hearing is not required unless the objectors raise "cogent factual objections to the settlement." *Id.* at

79; *Grinnell I*, 495 F.2d at 464 (objectors must make "clear and specific showing that vital material was ignored by the District Court").

Yet to survive appellate review, the district court must show it has explored comprehensively all relevant factors. *Protective Committee*, 390 U.S. at 434; *Plummer*, 668 F.2d at 659. Here, Judge Griesa adopted by reference the state court referee's report, making no independent findings of fact[4] or conclusions of law. It is thus the referee's report, not the district court's final judgment, that this court is in effect reviewing. The state court referee evaluated the fairness, reasonableness, and adequacy of the stipulated settlement under standards for settlement of New York derivative actions. Thus, he found that the settlement (1) accomplished substantially all the relief sought by the amended state complaint; (2) avoided the time and expense of trial; (3) resulted from arm's length, non-collusive negotiation; (4) provided appropriate injunctive relief; and (5) justifiably waived money damages, in view of the difficulty of proving individual claims, the uncertainty of success, the importance of the damage waiver to the settlement agreement, and adequacy of notice to the plaintiffs that their right to sue for damages had been waived.

Though the referee's report contained some useful analysis of the reasonableness of the settlement, and the District Judge was entitled to rely on pertinent portions of that report, his reliance could not substitute for federal court inquiry as to matters pertinent to the federal suit that were either not considered or inadequately considered by the referee. Moreover, the referee considered

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[4] He did ascertain that about 85% of plaintiffs' co-counsel's work was done in the state court proceedings.

some, but clearly not all, of the *Grinnell I* factors. His conclusions on damages, for example, may be misleading because he was assessing a state law breach of fiduciary duty/fraud claim, and not a federal law treble damages antitrust claim. At the very least as to that deficiency, the federal judge is required to hold a fairness hearing under *Plummer*. Finally, even if some relevant issues were considered by the referee, too many important questions were left open for us to approve Judge Griesa's adoption of the referee's conclusions. Our doubts fall under three broad headings.

Merits of plaintiffs' claims. The referee found that the plaintiffs' claims suffered enough defects on the merits that the waiver of damages in exchange for injunctive relief was appropriate. We are troubled by his ready acceptance of this proposition. For example, nowhere is there a useful discussion of the problems raised for the defense by the exclusive advertising arrangement enjoyed by CPG or of CPG's husbandry of the associations' membership lists and drives. Our conviction that the federal merits of the plaintiffs' claims must be carefully weighed is reinforced by the CPG defendants' quick capitulation allowing use of the complaint as a basis for settlement. CPG Brief at 40.[5]

Difficulty in proof of damages. Plaintiffs' attorneys' argument that damages were never sought because the costs of class notification would be prohibitive ignores *Oppenheimer Fund, Inc. v. Sanders*, 437 U.S. 340

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5 We do not intend to imply that quick settlements should be viewed with heightened suspicion; few cases will seek to dispose of the rights of so many persons who are not active participants in a suit on the basis of as little vigorous presettlement investigation of the merits of their claims as this one.

(1978), where the Court flexibly construed the principle of *Eisen v. Carlisle & Jacquelin*, 417 U.S. 156, 178-79 (1977), that a party must bear the "burden of financing his own suit," and noted instances where it may be proper for a district court to require the defendant to bear the costs of class notifications. *Oppenheimer Fund Inc.*, *supra*, at 356-59. Here, the associations and CPG were apparently able to perform notification with less difficulty and expense than the class plaintiffs, and the court could have exercised discretion under Fed. R. Civ. P. 23(d) to order, as ultimately happened, that notice be sent through the associations' membership magazines, or that the magazine must accept paid advertisements by class plaintiffs.

The referee's argument that waiver of damage claims was appropriate because proof of individual claimants' damages would be difficult is, as noted, not premised on federal antitrust laws where total damages may be three times as great and where means may be available to assess the harm to the class even if proof of each plaintiff's damages would be difficult. More tellingly, it fails to address specifically the possibility that plaintiffs' loss could be measured as CPG's excess gain, *see Zeller v. Bogue Electric Manufacturing Corp.*, 476 F.2d 795, 802 (2d Cir.), *cert. denied*, 414 U.S. 908 (1973), a possibility that cannot be dismissed or simply overlooked in light of the statements in plaintiffs' counsels' affidavit that CPG's arrangement with the associations was very profitable, that "the opening of competitive bidding for the Associations' $270 million annual group health insurance has resulted in increasing the cash payout of group health insurance benefits to class members by over $39 million per annum" and that opening the associations' publications to other advertisers will increase advertising reve-

nues by "over $19 million" in "the next five years alone." Lastly, the referee's dismissal of the *Copitka* case because of the peculiarities of California's punitive damages law only has a bearing on the New York state law fraud claims. It says nothing about suits brought in other states or under the federal antitrust laws when actual damages may be trebled. The bearing of the *Copitka* settlement on possible federal claims and whether notice of that settlement to the class members is sufficient to nullify its impact on the fairness of the settlement must also be reconsidered.

Fees. Judge Griesa's failure independently to investigate the issue of counsel fees leaves us with a sense of uneasiness, as the Judge left unanswered several important questions, including:

Why was a bonus awarded so large as to produce a total fee award that amounts to double the usual rates for counsel—for a total of approximately $240 per hour—regardless of the difficulty of the tasks performed?

What difficulty was involved that was extraordinary?

Why was all the time necessary for the mere pursuit of injunctive relief to which there was such rapid agreement in principle?

Was the recital of the draft proposal of defendants to the effect that plaintiffs' counsel had researched the legal principles applied to damage claims dropped in the executed stipulation and, if so, why?

Were the fees agreed upon before the settlement was reached or only after substantive issues were worked out?

Why were the associations to pay any part of the bill since the gravamen of the complaints was that the associations (or their members) had lost money by virtue of CPG's actions?

A federal court approving the award of fees in this situation, where state and federal suits are being settled in one agreement, must make its own independent valuation of fairness and reasonableness; it cannot simply rely on the state referee's.[6]

Reversed and remanded for proceedings in accordance with this opinion.

NEWMAN, *Circuit Judge*, concurring:

I concur in Judge Oakes' comprehensive opinion and add a few words only to fill out the context in which the settlement was reached and to emphasize that our concern for more detailed analysis by the District Judge is not an intimation either way as to whether or not the settlement should be approved. The Associations had entered into an exclusive arrangement with the Colonial Penn Group at a time when no other insurer appeared willing to write group health insurance policies for the elderly. The risk that CPG took turned out to be advantageous for it, and it made substantial profits. Once the profitability of this type of insurance was demonstrated, the continued existence of an exclusive arrangement between the Associations and CPG was no longer in the best interests of the Associations' members. Whether the arangement ever was, or at some point might have become, unlawful is, of course, quite a different matter. In any event, the Associations and CPG, no doubt prodded by the initiation of state and federal lawsuits, agreed in September 1980 to

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6 In fairness to the district judge, he did insist on making an independent evaluation. He simply left unanswered certain questions, the answers to which are necessary for purposes of our review.